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IN THE

SUPREME COURT OF THE UNITED STATES

October Term, 1975

No. 75-1524

TRUSTEES OF THE READING BODY WORKS, INC. PROFIT SHARING PLAN TRUST, *Petitioners*

v.

SECURITIES INVESTOR PROTECTION CORPORATION, *et al.*, *Respondent*

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

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IN THE
SUPREME COURT OF THE UNITED STATES

October Term, 1975

No.

Trustees of the Reading Body Works, Inc.
Profit Sharing Plan Trust, *Petitioners*

v.

Securities Investor Protection Corporation, *et al.*,
Respondent

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

The Trustees of the Reading Body Works, Inc. Profit Sharing Plan Trust, on behalf of the several beneficiaries of said Trust, the Petitioners herein, pray that a writ of certiorari issue to review the opinion and judgment of the United States Court of Appeals for the Second Circuit entered on January 23, 1976.

FILED THROUGH

OPINIONS BELOW

The opinion of the Bankruptcy Court of the United States District Court for the Southern District of New York granting Petitioners' claim is printed at page 26 of the Appendix hereto and is reported unofficially at CCH Fed. Sec. L. Rptr., 74-75 Transfer Binder, ¶94,972. The opinion of the United States District Court for the Southern District of New York affirming the decision of the Bankruptcy Court is printed at page 33 of the Appendix hereto and is reported unofficially at CCH Fed. Sec. L. Rptr. ¶95,228. The opinion of the Court of Appeals which reversed the judgment of the District Court is printed at page 36 of the Appendix hereto. It has not yet been reported in the official reports but is reported unofficially at CCH Fed. Sec. L. Rptr. ¶95,426.

JURISDICTION

The judgment of the United States Court of Appeals for the Second Circuit was entered on January 23, 1976. Rehearing was not sought. The jurisdiction of this Court is invoked under 28 U.S.C. §1254(1).

QUESTIONS PRESENTED

In a proceeding to liquidate a broker-dealer under the Securities Investor Protection Act of 1970 ("1970 Act"),[1] the Securities Investor Protection Corporation ("SIPC") provides "financial relief to the customers of failing broker-dealers with whom they had left cash or securities on deposit." *SIPC v. Barbour*, 421 U.S. 412, 95 S.Ct. 1733, 1735, 44 L.Ed. 2d 263 (1975). The Petitioners

1. 15 U.S.C. § 78fff(a), 78fff(c)(2)(A)(ii), 78fff(c)(2)(A)(iv) and 78fff(f)(1).

submitted a claim for cash and securities in such a liquidation proceeding on behalf of each of the 108 beneficiaries of a profit sharing plan trust who maintained an account with the debtor.[2] Both the Bankruptcy Court and District Court agreed that each beneficiary was within the 1970 Act's definition of "customer" and entitled to recovery. The Court of Appeals has reversed this decision and remanded to the Bankruptcy Court. The questions presented on this appeal are:

1. Does the limitation on the federal statutory insurance protection of customers of insolvent broker-dealers mean that the vested rights of a group of employees in a profit sharing retirement fund are insured as only one customer?

2. Alternatively, does each of the three trustees who dealt with the broker qualify as a separate "customer" of the insolvent broker-dealer entitled to the statutory coverage?

STATUTES INVOLVED

Because of their length, the following statutes which are involved are set forth at pages 56-58 of the Appendix: Sections 6(a), 6(c)(2)(A)(ii) and (iv) and 6f(1) of the 1970 Act.[3]

STATEMENT OF THE CASE

In 1957 Reading Body Works, Inc. ("Reading") established a profit-sharing plan (the "Plan"), pursuant to which a trust fund was created and maintained through yearly employer contributions based upon Reading's net

2. Petitioners' claim is reproduced as an exhibit to the Application of Bondy in the Appendix.

3. 15 U.S.C. §78aaa *et seq.*

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earnings. The Plan provided that employees would earn "credits" or a percentage interest in the fund according to annual compensation level and consecutive years of service. The employees' individual credit units were in proportion to the units of all employees, and were based upon the current value of the assets in the trust. Separate accounts for each employee were maintained in the records of the trust to reflect the individual employee's accumulated credits and the current value of each employee's account. Each employee's interest in the trust was vested, non-forfeitable and was payable upon the employee's termination of employment with Reading. Three trustees (the "Trustees") were responsible for the management of the trust and the investment of its assets.

In 1972, an account was established with Morgan, Kennedy & Co. (the debtor) in the Trustees' names on behalf of the Trust's beneficiaries. The Trustees made investment decisions and communicated regularly with the debtor with respect to all transactions.

Liquidation proceedings against the debtor were commenced under the 1970 Act in 1973, and a trustee (Bondy) was appointed. The Plan's Trustees subsequently submitted a claim for cash and securities on behalf of the beneficiaries for $133,051.15.[4]

Bondy thereafter informed SIPC that he intended to treat the 108 trust beneficiaries as separate customers of the debtor; this would entitle each of the 108 to the 1970 Act's maximum insurance coverage per customer of $50,000 for securities and $20,000 for cash held by the debtor as of the date of commencement of liquidation proceedings. The Trustees supported Bondy's position; they also argued alternatively that, if the 108 beneficiaries were not "customers" of the debtor, then the three Trustees

4. The claim, as submitted, was for $133,236.15. (The difference, $181.00, resulted from an error in computing interest on a Treasury Bill purchased in the account; this latter amount is not in issue here.)

should be treated as separate customers, and the claims accorded the maximum award for cash and securities held by the debtor.

Bondy's interpretation of the term "customer" was disputed by SIPC. SIPC claimed that the trust (or the Trustees collectively), and not each of its beneficiaries, was the debtor's customer under the 1970 Act; accordingly, SIPC recognized only one valid claim for cash.

Both the Bankruptcy Court and the District Court ruled in favor of Bondy and the Trustees on the issue of the definition of "customer" and did not reach an unrelated argument raised by the Trustees. The Court of Appeals reversed the District Court on the issue of the definition of "customer" and remanded the case for a determination of the other argument raised by the Trustees. That argument relates to a potential securities claim and has nothing to do with the finality of the issue here involved.

REASONS FOR GRANTING THE WRIT

The Court of Appeals has decided an important question of federal law which has not been, but should be, settled by the Supreme Court. The interpretation adopted by the Court of Appeals with respect to who is a "customer" of an insolvent broker-dealer unnaturally restricts the coverage of a remedial statute enacted to benefit a class of public investors which includes the beneficiaries of a profit sharing plan trust.

Congress has manifested a special regard for the protection of employer funds by the Employee Retirement Income Security Act of 1974.[5] It recognized that the nature of a profit sharing plan is such that it is a collection of individual accounts identifiable to specific participants and their beneficiaries.[6] In the 1970 Act, Congress has provided

5. 29 U.S.C. §1001, *et seq.*

6. 29 U.S.C. §1107(d)(3)(A).

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for the insurance protection of cash and securities of customers held by brokers. This Court should not let stand a significant precedent which departs from a basic congressional objective in protecting funds held essentially for the ultimate retirement of employees. Insurance protection should cover those who need it, and should not be arbitrarily limited by alleged concepts or principles that are unrelated to the basic purposes of insurance. The decision of the Court of Appeals denies the existence of the individual beneficiaries' ownership interest in the cash and securities held by their insolvent broker-dealer and, therefore, conflicts with this related statute.

In addition, the decision of the Court of Appeals denying recovery to the beneficiaries upon the insolvency of their broker-dealer conflicts with a similar Congressional scheme providing recovery to beneficiaries of trust accounts who have incurred losses as a result of the insolvency of their insured bank or savings institution. The Federal Deposit Insurance Act[7] and the Federal Savings and Loan Insurance Act[8], which the legislative history of the 1970 Act recognizes as models of protection[9], would clearly provide a full recovery to the beneficiaries on the instant claim. Both FDIA and FSLIA provide coverage to "insured deposits" (or "insured accounts")[10] which are defined by regulation to include the individual interests of identifiable beneficiaries. This is analogous to the 1970 Act which extends insurance protection to "customers" and which should also be construed to include ascertainable beneficiaries.

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7. 12 U.S.C. §1811 *et seq.*

8. 12 U.S.C. §1724 *et seq.*

9. See House Report No. 91-1613, October 21, 1970, in U.S. CODE CONGRESSIONAL AND ADMINISTRATIVE NEWS, 91st CONGRESS, 2d Sess. 1970, at p. 5255.

10. 12 U.S.C. §1813(m); 12 U.S.C. §1724(c).

Section 6(c)(2)(A)(ii)[11] of the 1970 Act defines "customers" of a debtor as:

> ". . . persons (including persons with whom the debtor deals as principal or agent) who have claims on account of securities received, acquired or held by the debtor from or for the account of such persons . . . and shall include persons who have claims against the debtor arising out of sales or conversions of such securities. . . ."

This definition of "customer" was taken with slight modification from Section 60e of the Bankruptcy Act which deals specifically with stockbroker insolvency and bankruptcy.[12] There are two basic differences between the two definitions: One, the 1970 Act recognizes that the debtor may act as a principal or dealer, avoiding the result of *Gordon v. Spalding*, 268 F.2d 327 (5th Cir. 1959); Two, persons who deposited "cash" with the debtor for the purchase of securities are included among customers. In a separate provision of the statute[13], general partners, officers and directors of the debtor, *inter alia*, are specifically excluded from the definition's coverage as "customers."

Unfortunately, there are no cases interpreting Section 60e's definition of "customer" and the cases examining the 1970 Act's definition of "customer" involve such distinguishable facts that they offer little guidance to the

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11. U.S.C. §78fff(c)(2)(A)(ii).

12. 11 U.S.C. §96e(1); that section provides that ". . . 'customers' of a stockbroker shall include persons who have claims on account of securities received, acquired, or held by the stockbroker from or for the account of such persons . . . and shall include persons who have claims against the stockbroker arising out of sales or conversions of such securities";

13. 15 U.S.C. §78fff(f)(1)(C).

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question before this court.[14] While the fact situation presented in this case has not arisen with regularity in broker-dealer insolvencies,[15] the ambiguity surrounding the statutory definition and the related scope of coverage can and will recur and hence merits review by this Court.

The 1970 Act does not supersede Section 60e of the Bankruptcy Act as it does not discharge the debts of an insolvent stockbroker. Instead, it provides a special liquidation proceeding in which an appointed trustee returns specifically identifiable property to the debtor's customers; marshals and supplements, when necessary, the debtor's assets by advances from SIPC; and distributes these funds to the debtor's customers. In addition, the trustee is authorized to complete certain open transactions at the date of insolvency.

Upon a stockbroker's insolvency, Section 60e of the Bankruptcy Act [11 U.S.C. §96e(2)] permitted a customer's recovery of specifically identifiable property. The same is true under the 1970 Act [§78fff(a)(1)(A)]. Under both statutes, if the Petitioners' claim was for securities that were in the debtor's possession at the filing date and re-

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14. See, *e.g.*, *S.E.C. v. First Securities Co. of Chicago*, 507 F.2d 417, 421-422 (7th Cir. 1974) (claimants were not "customers" since they entrusted their securities to Nay, not to First Securities); *S.E.C. v. Packer, Wilbur & Co.*, 498 F.2d 978, 984 (2d Cir. 1974) (only "innocent" customers may claim protection under the Act); *S.E.C. v. F.O. Baroff Company, Inc.*, 497 F.2d 280, 283 (2d Cir. 1974) (individual's loan of securities to a failing brokerage house had nothing to do with investment, trading or participation in the securities market); *S.E.C. v. Alan F. Hughes, Inc.*, 461 F.2d 974, 977 (2d Cir. 1972) (opinion's opening sentence declares that the Act's purpose is to protect public customers in the event broker-dealers with whom they transact business encounter financial difficulties).

15. Petitioners are aware of one other case involving a similar claim; see *In re Weis Securities, Inc., (Claim of McGrath)*, CCH Fed. Sec. L. Rptr., 74-75 Transfer Binder, ¶95,061 (S.D.N.Y. March 27, 1975).

mained specifically identifiable, such securities would have been recoverable. The same result would follow whether or not the claiming customer was a single person or 108 persons.

Under both statutory systems, after the "specifically identifiable property" has been recovered from the debtor's estate, all remaining property at any time received, acquired or held by the stockbroker from or for the account of customers is considered to be a "single and separate fund."[16] Under Section 60e, all other customers (except those who are entitled to immediate possession of specifically identifiable securities without the payment of any sum to the stockbroker) comprised a single and separate class of creditors, who, following payment of administrative expenses, shared ratably in such fund on the basis of their respective net equities as of the date of bankruptcy. The concept of net equity was directly related to the account balances.

It is at this point that the major difference introduced by the 1970 Act becomes significant: the SIPC advances.[17] Instead of being restricted to distributing equitably the *actual* cash and securities in the debtor's possession at the commencement of the proceedings, customers are entitled to benefit from the cash advances of SIPC to the debtor's estate. Through this form of insurance they are permitted to recoup losses, up to prescribed limits, based upon their status as "customers" rather than upon the standard employed by former Section 60e, *viz.*, their account or net equity. Contrary to the underlying premise of the opinion of the Court of Appeals in this matter, SIPC protects *customers, not accounts*.

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16. 11 U.S.C. §96e(2); 15 U.S.C. 78fff(c)(2)(B).

17. 15 U.S.C. §78fff(f)(1), which provides, *inter alia*, "In order to provide for prompt payment and satisfaction of the net equities of customers of debtor, SIPC shall advance to the trustee such moneys as may be required to pay or otherwise satisfy claims in full of each customer, but not to exceed $50,000 for such customer. . . ."

It is apparent that the 1970 Act does not expressly designate the beneficiaries of a profit sharing plan as customers of a broker-dealer who are entitled to statutory recovery. Consequently, an analysis of the question presented in this Petition, whether the trust's beneficiaries (or, at least, the three Trustees) are customers with a right of recovery under the 1970 Act, may be assisted by reference to several recent cases in this Court concerning whether a private remedy is implicit in a statute not expressly providing for one.[18] At least three of the four criteria outlined by this Court in *Cort*, *SIPC* and *Amtrak* are helpful:[19] (1) whether the statute was designed to protect a class of persons, including the beneficiaries of a profit sharing plan (or the three Trustees), from losses arising through the insolvency of their broker; (2) whether there is any indication of legislative intent to create or deny recovery; and (3) whether implication of a right of recovery would be consistent with the underlying purposes of the legislative scheme.

(1) Whether the 1970 Act was designed to protect a class of persons, including the beneficiaries of a profit sharing plan (or the three Trustees), from losses arising through the insolvency of their broker?

In *SIPC v. Barbour*, *supra*, this Court reviewed the factors which led to the passage of the 1970 Act and the purposes that it was intended to accomplish. 95 S.Ct. at 1736, 1739. This is significant because "rather large inter-

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18. See *Cort v. Ash*, 422 U.S. 66, 95 S.Ct. 2080, 2087-88, 45 L.Ed.2d 26 (1975); *SIPC v. Barbour*, 421 U.S. 412, 95 S.Ct. 1733, 45 L.Ed.2d 263 (1975); and *National Rail Passenger Corp. v. National Association of Rail Passengers*, 414 U.S. 453, 94 S.Ct. 690, 38 L.Ed.2d 646 (1974) ("Amtrak").

19. The fourth criterion, whether the cause of action is one traditionally relegated to state law such that inference of a federal cause of action would be inappropriate, has no relevance in this inquiry.

stices (remain) in the Act resulting in part from engraftment of insurance provisions upon the preexisting Section 60e bankruptcy provisions applicable to stockbrokers." *SEC v. Aberdeen Securities Co., Inc.*, 480 F.2d 1121, 1123 (3d Cir. 1973).

The basic definition of "customers" in both the 1970 Act and Section 60e is persons who have *claims against the debtor* on account of securities or cash received, acquired or held by the now-insolvent broker. Both the Bankruptcy Court[20] and the District Court [21] found the beneficiaries to be customers having claims against their broker. These Courts effectively found that the claiming hourly and salaried employees, the welders, clerks and managers of Reading, are among the very people whom Congress sought to protect from the financial collapse of their broker-dealer.

Although each of the 108 beneficiaries had a vested and ascertainable interest in the account and, consequently, is a person who has a "claim" against the debtor, the opinion of the Court of Appeals denied that the beneficiaries were among included "customers" by asserting that the "beneficiaries were neither investors nor traders" and possessed none of the required attributes for customer status under the 1970 Act.[22] This conclusion is contrary to fact and law.

A qualified profit sharing plan such as that maintained by Reading is a form of deferred compensation to an employee and is, in reality, a collection of individual accounts combined for purposes of administration, and referred to in ERISA as an "eligible individual account plan."[23] The employer's contributions to the trust are gener-

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20. Opinion of Bankruptcy Judge Babitt at pages 28-29 of the Appendix.

21. Opinion of Judge Frankel at page 33 of the Appendix.

22. Opinion of Court of Appeals at Appendix pages 42-44.

23. 29 U.S.C. §1107(d)(3)(A).

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ally deductible for Federal income tax purposes when made, but the employee-beneficiaries are not taxed on these contributions (or any income accumulated thereon) until the trust funds are distributable in accordance with the terms of the plan.[24] The funds or investments within the trust are held for the exclusive benefit of the individual beneficiaries in order for the plan to maintain its qualified status for tax purposes. Amounts contributed to the trust must be set apart in the accounts of individual participants pursuant to a definite allocation formula. Income and expenses of the trust are similarly allocated to the individual accounts.

The beneficiaries did "invest and trade" with a broker in the only form available to them, i.e., through the Trustees' directions to their broker. The suggestion that each beneficiary could not buy or sell a particular security is not a criterion of exclusion for a "customer." However, the fact that each beneficiary has a claim in a definite amount against the stockbroker on account of transactions conducted on his behalf is a criterion of inclusion.

Petitioners' alternative argument that the three Trustees be considered as "customers" of the debtor was also dismissed by the Court of Appeals.[25] Yet it was the three Trustees who opened the account with the debtor, who transmitted orders and payments to the debtor, executed the share certificates for transfer, and finally submitted the claim on behalf of the several beneficiaries. If the beneficiaries are not found to be "customers" within the 1970 Act because of their remoteness from the debtor, no similar exclusion should be asserted against the Trustees. At least they should be considered to be "traders and investors."

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24. See, generally, 26 U.S.C. §401 and Regulations thereunder.

25. Opinion of the Court of Appeals at Appendix pages 49-52.

There is no authority in SIPC to count three Trustees, who trade the account, as only one customer. The Court of Appeals stated that the "number of trustees sharing this responsibility was fortuitous."[26] Yet, it is the concept of the Court of Appeals that compels Petitioners to maintain this alternative argument; if the 108 beneficiaries cannot be customers because they are "neither investors nor traders," then the three Trustees who did the investing and trading must be the "customers." They have submitted claims upon their separate status as "customers" and should be entitled to recovery.

(2) Whether there is any indication of legislative intent to create or deny recovery to beneficiaries of a profit sharing plan?

The legislative history indicates that little attention was paid to the 1970 Act's definition of customer.[27] With the exception of the two differences noted at p. 6, *supra*, Congress incorporated the definition of "customer" from Section 60e of the Bankruptcy Act.

It seems plain that Congress was attempting to protect the greatest number of individuals involved with the securities markets rather than the greatest number of dollars invested.[28] By allowing customer status to each small investor-beneficiary of the profit sharing plan, this intent will be carried out. After all, "(W)ords must be construed

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26. Opinion of the Court of Appeals at Appendix page 52.

27. House Report No. 91-1613, October 21, 1970, in U.S. CODE CONGRESSIONAL AND ADMINISTRATIVE NEWS, 91st CONGRESS, 2d SESS. 1970, p. 5254, *et seq*.

28. The opinion of the Court of Appeals noted that while SIPC is designed to protect customer losses up to $50,000, more than 90% of the total dollar value of all accounts at the time the 1970 Act was enacted contained more than $50,000. *Id*, at page 51 of the Appendix. See Guttman, "Broker-Dealer Bankruptcies", 48 N.Y.U.L.R. 887, 909 (November 1973).

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to carry out the manifest intent of the Congress and in all cases shall be construed in the sense which best harmonizes with the context and promotes to the fullest extent the desired objective." *In re McMillan, Rapp & Co., Claim of Freeman*, 38 F. Supp. 40, 41, *aff'd*, at 123 F.2d 428 (3d Cir. 1941).

(3) Whether implication of a right of recovery would be consistent with the purposes of the legislative scheme?

In *SIPC v. Barbour, supra*, this Court noted that "Congress' primary purpose in enacting the SIPA and creating SIPC was, of course, the protection of investors." 95 S.Ct. at 1739. The recognition of a right of recovery on behalf of each beneficiary will further that goal. Because of the vested nature of the beneficiaries' interest in the trust assets lost through insolvency of the debtor, their protection as investors and customers will not exceed the statutory limits.

In the only other case which Petitioners have discovered with similar facts and reasoning to the instant case, *In re Weis Securities, Inc. (Claim of Mc Grath)*, CCH Fed. Sec. L. Rptr., 74-75 Transfer Binder ¶95,061 (S.D.N.Y. March 27, 1975), the failure to define a trust's beneficiary as the "customer" would have permitted the evasion of a specific exclusion from the 1970 Act's coverage. The claimant in that case, an Executive Vice-President of the debtor, was the principal beneficiary of a trust account maintained at the debtor. Upon the institution of a SIPC proceeding, the trust submitted a claim for cash which was rejected by Bankruptcy Judge Babitt. He held that the beneficiary, not the trust, was the customer of the debtor and that the beneficiary-customer was specifically excluded from the 1970 Act's coverage by Section 6(f)(1)(C)'s prohibition against advances to general partners, officers or directors of a debtor.

But for Judge Babitt's holding in that case, the trust for the benefit of the individual excluded by the statute,

under the present holding of this Court of Appeals, would have received full reimbursement out of SIPC funds despite the 1970 Act's explicit provisions to the contrary.

Other analogous statutory schemes would permit recovery by a trust beneficiary in the circumstances of this case. Both the Federal Deposit Insurance Act (12 U.S.C. §§1811, *et seq.*) and the Federal Savings and Loan Insurance Act (12 U.S.C. §1724, *et seq.*) by means of regulations promulgated thereunder[29] carry out the scheme of separate coverage for each beneficiary of a trust which maintains an account at an insured institution. The Securities Exchange Act of 1934, to which the 1970 Act is to be considered an amendment,[30] has been held to permit a trust beneficiary to bring a separate cause of action. See *James v. Gerber Products Co.*, 483 F.2d 944, 949 (6th Cir. 1973). Finally, Section 502 (29 U.S.C. §1132) of the Employee Retirement Income Security Act of 1974 (29 U.S.C. §§1001, *et seq.*) ("ERISA") expressly permits the beneficiaries of a profit sharing plan to sue for various kinds of relief.

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29. 12 CFR §§330, *et seq.* and 12 CFR §§546, *et seq.*

30. 15 U.S.C. §78bbb; see *S.E.C. v. Packer, Wilbur & Co., Inc.*, *supra*, at 985.

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CONCLUSION

For the reasons set forth above, it is respectfully submitted that this petition for a writ of certiorari should be granted to review the opinion and judgment of the Court of Appeals.

Respectfully submitted,

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APPENDIX

A1
Application of Eugene L. Bondy, Jr.

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

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73 Civil 1057 (RB)

SECURITIES INVESTOR PROTECTION CORPORATION, *Applicant*
SECURITIES AND EXCHANGE COMMISSION, *Plaintiff*

against

MORGAN, KENNEDY & CO., INC.;
IRWIN RUDNET AND GERALD RUDNET, *Defendants*

STATE OF NEW YORK,
COUNTY OF NEW YORK, *ss:*

APPLICATION

EUGENE L. BONDY, JR., being duly sworn, deposes and says:

1. On March 13, 1973, by Order of the Honorable Marvin E. Frankel, United States District Court Judge for the Southern District of New York, I was appointed Trustee ("Trustee") for the liquidation of the business of Morgan, Kennedy & Co., Inc. (the "Debtor"), with all the duties and powers of a trustee prescribed in the Securities Investor Protection Act of 1970 (the "1970 Act").

2. This Application is being made for an Order (the form of which is annexed hereto) which would:

(a) designate the claim of the Trustess of the Reading Body Works, Inc. Profit Sharing Plan Trust (the "Trust") against the Debtor for $133,051.15 to be

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the individual claims of the 108 individual beneficiaries of the Trust; and

(b) order that under §6(c)(2)(A)(ii) of the 1970 Act each of the individual beneficiaries of the Trust is a separate "customer" and thus entitled to the $20,000 maximum coverage provided for in §6(f) of the Act.

3. This Application also seeks an Order (in the form annexed hereto) to make an interim advance of $20,000 to the Trust pending a final decision of the Trust's entire $133,051.15 claim.

4. On April 5, 1957 the Reading Body Works, Inc. (the "Company") established the Reading Body Works, Inc. Profit Sharing Plan (the "Profit Sharing Plan"). Thereafter, on April 12, 1957, the Company and three individual Trustees ("the Trustees") entered into an Agreement and Declaration of Trust for the benefit of the individual employees of the Company.

5. Under the terms of the Profit Sharing Plan, yearly contributions are made by the Company to the Trust for the benefit of the Company's employees based upon the Company's yearly net earnings. Each employee accumulates "credits" or a percentage interest in the fund according to his (or her) annual compensation level and consecutive years of service. The Agreement and Declaration of Trust specifically require that a separate "account" be maintained for each employee to which is credited his proportionate share of the Company's yearly contribution and any increase in the market value of the trust fund. Each employee is given a non-forfeitable vested interest in the amounts allocated to his account which is received, according to certain conditions upon the termination of employment with the Company.

6. The Trust became a customer of the Debtor in December, 1972 as part of the transfer of customer accounts from Monaghan & Company, Inc., a broker-dealer whose business had been acquired by the Debtor. The Trust's account was handled by Frederick Garfinkle, a registered representative associated with the Debtor.

7. During the months of January and February of 1973 the Trustees authorized the Debtor to execute the sales of certain securites on behalf of the Trust. These securities were delivered to the Debtor in order to complete these sales. However, although the sales were completed by the Debtor, no part of the proceeds from them were ever paid to the Trust. The net proceeds from such sales totaled $83,051.15, and this amount was credited to the account of the Trust on the books and records of the Debtor. On March 9, 1973, the filing date of this liquidation proceeding, these securities were being held by the Chemical Bank for clearance and transfer and efforts to recover them by the Trust have thus far been unsuccessful.

8. On February 7, 1973 the Debtor purchased, with free credit balance funds belonging to the Trust, a United States Treasury bill in the face amount of $50,000. This treasury bill was fraudulently and illegally hypothecated with the Chemical Bank and its proceeds, which were credited against the Debtor's loan account by the Chemical Bank were never received by the Trust.

9. By reason of the foregoing, a credit balance in the amount of $133,051.15 was owing to the Trust on March 9, 1973, the date of bankruptcy of the Debtor. (A copy of the Trust's customer account statement for March, 1973 is annexed hereto as Exhibit A).

10. By complaint dated June 7, 1973, the Trustees brought an action against the PBW Stock Exchange, Inc.,

the Chemical Bank, Irwin Rudnet, Gerald Rudnet, and Frederick Garfinkle, seeking to recover the above amount. This action was based upon alleged violations of the law committed by the persons named in the complaint. At this date, no recovery has been had in ths action by the Trust.

11. By letter dated June 26, 1973 counsel for the Trustees made formal claim upon the Debtor on behalf of each of the beneficiaries of the Trust. The Claim (a copy of which is annexed hereto as Exhibit B), dated June 20, 1973, asked for money balances as of March 9, 1973 in the amount of $133,236.15.* Attached to the claim was a memorandum (a copy of which is annexed hereto as Exhibit C) which sets forth the individual transactions, including that concerning the proceeds of the $50,000 face amount treasury bill, which gave rise to the claim.

12. By letter dated October 9, 1973 (a copy of which is annexed hereto as Exhibit D), the Trustee informed the Securties Investor Protection Corporation ("SIPC") that he considered each of the 108 beneficiaries of the Trust a separate "customer" within the meaning of §6(c)(2)(A)(ii) of the 1970 Act and therefore each entitled to the maximum dollar limitation provided in §6(f) thereof. The Trustee based his conclusion in part upon a memorandum of law which had been prepared by his counsel (a copy of which is annexed hereto as Exhibit E).

13. On March 6, 1974 William Ragusin, the liquidator of the Debtor, on behalf of the Trustee, filed a Proof of Claim with the Insurance Company of North America ("INA") making claim under a broker's blanket bond

---

* The $181 difference between this figure and the amount of the advance sought by the Trustee results from a revision of the Trust's initial estimate of the value of the $50,000 treasury bill.

which had been maintained by the Debtor. This claim alleged that the failure of the Debtor to pay the proceeds of the $50,000 treasury bill to the Trust was the direct result of the illegal and fraudulent conduct of certain of the employees of the Debtor and that therefore the Trustee should be reimbursed by INA under the terms of the broker's blanket bond for the loss resulting from this dishonest conduct. INA is now investigating this claim but has thus far given no indication of an intention to pay it.

14. By letter dated May 22, 1974 counsel for the Trustee sent a Trustee's Request for SIPC Advance for Payments to Customers dated May 17, 1974 (a copy of which is annexed hereto as Exhibit F), to SIPC requesting an advance in the amount of $133,051.15. This request was based upon the Trustee's previous position that each of the 108 individual beneficiaries of the Trust should be considered a separate customer under §6(c)(2)(A)(ii). Counsel for the Trustee also requested that if SIPC decided to deny the request for the full amount, it forward $20,000 in cash as an interim advance. There is no dispute between SIPC and the Trustee that the Trust is entitled to at least $20,000 in satisfaction of its claim.

15. By letters dated May 23, 1974 and June 10, 1974 (copies of which are annexed hereto as Exhibits G and H), counsel for SIPC informed the Trustee that it would not treat the claim of the Trust as the claim of 108 separate customers of the Debtor and therefore would not advance the full amount of the Trust's claim.

16. By letter dated June 28, 1974 (a copy of which is annexed hereto as Exhibit I), Thomas R. Cassella, a

manager of operations associated with SIPC, returned the Request for Advance dated May 17, 1974 to the Trustee stating that the request had not been approved for payment. Mr. Cassella also stated that a separate court order would be necessary before the $20,000 interim payment could be advanced.

17. The Trustee has given careful consideration to the claim of the Trust and has determined after reviewing the advice of his counsel contained in the memorandum of law dated October 5, 1973 (Exhibit E) as well as the letter stating the position of SIPC dated May 23, 1974, (Exhibit G), that the individual beneficiaries of the Trust are each entitled to protection as individual customers under the 1970 Act.

18. If the claim of the Trust is paid in full, every claim filed by a customer which has not been found objectionable by the Trustee and disallowed by a court order will have been satisfied in full.

19. The Trustee believes that the spirit of the 1970 Act and the interests of justice require that this claim be paid. The beneficiaries of the Trust are factory workers whose savings make up the funds which were invested by the Trust. Congress was concerned with protecting this very class of small investors when it enacted the 1970 Act.

20. As it pointed out in the memorandum of law annexed hereto as Exhibit E, neither the 1970 Act nor the series 100 rules promulgated thereunder by SIPC give a definite answer to the treatment to be accorded the beneficiaries of trusts under the 1970 Act. The Trustee feels that since the 1970 Act was to have the same purpose and

effect as the Federal Deposit Insurance Act and the Federal Savings and Loan Insurance Act, and since the regulations promulgated under both of those acts provide separate protection for each beneficiary of a trust maintaining a deposit with an insured institution, the same kind of protection should be available to investors maintaining accounts with broker-dealers who have become insolvent.

Dated: New York, New York
September 5, 1974

/s/ EUGENE L. BONDY, JR.
Eugene L. Bondy, Jr.

(Subscription omitted in printing)

(Exhibits D, E, G and H omitted in printing)

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morgan, kennedy & co., inc.
Member N.Y., Philadelphia - Baltimore - Washington Stock Exchange

- 5 Hanover Sq New York, New York 10004 • (212) 24[illegible]480
- Hitching Post Inn, Box 358 Chambersburg, Pa. 17201
- 301 Arthur Godfrey Rd., Miami Beach, Florida 33140

YOUR ACCOUNT NO. | TYPE | SAC
32-00862 | 1 | 095

YOUR TAXPAYER IDENTIFICATION NUMBER

TTEES FCR READING BCCY WORKS
PROFIT SHARING PLAN
DTD 4/12/57 PARAMETRICS
420 GREGG AVE PO BCX 14
READING PA 19603

PERIOD ENDING 03/30/73

PAGE # 1

DATE	DELIVERED OR RECEIVED	SOLD OR BOUGHT	DESCRIPTION	CREDIT OR DEBIT	AMOUNT CREDITED TO OR DEBITED TO YOUR ACCOUNT	AMOUNT CREDITED TO OR DEBITED FROM YOUR ACCOUNT	NET CREDIT OR DEBIT BALANCE
			BAL FWD FEB 28				83,051.15CR
03/05/73			SGM USTEAS R	CR		50,000.00	
			CLOSING BALANCE MAR 30				133,051.15CR
			POSITIONS				
03/30/73	200		HOFFMAN ELECTRONICS				
03/30/73	~~50,000~~		US TREASURY BILL ~~5.40 DUE 3/1?1973~~				

IF THIS STATEMENT IS NOT CORRECT AS INDICATED ABOVE, PLEASE RETURN IT IMMEDIATELY

PLEASE RETAIN THIS STATEMENT FOR INCOME TAX PURPOSES. A CHARGE WILL BE MADE FOR ADDITIONAL COPIES.

"ANY FREE CREDIT BALANCE CARRIED BY MORGAN, KENNEDY & CO., INC. FOR YOUR ACCOUNT REPRESENTS FUNDS PAYABLE UPON DEMAND WHICH, ALTHOUGH PROPERLY ACCOUNTED FOR ON OUR BOOKS OF RECORD, ARE NOT SEGREGATED AND MAY BE USED IN THE CONDUCT OF OUR BUSINESS."

EXHIBIT B

MORGAN, KENNEDY & CO., INC.
IN LIQUIDATION UNDER THE SECURITIES INVESTOR PROTECTION ACT OF 1970
EUGENE L. BONDY, JR., TRUSTEE

NOTE: THIS CLAIM FORM MUST BE COMPLETED AND FILED BY CUSTOMERS WHO HAVE CLAIMS FOR CASH OR SECURITIES, OR BOTH. IF NO CLAIM IS FILED BY JUNE 29,1973 THE TRUSTEE WILL ASSUME THAT THERE IS NO CLAIM.

32-00662
32-11674

Irving Suknow, Herbert Ostroff, and Doris Rauenzahn, Trustees for the Reading Body Works, Inc. Profit Sharing Plan Trust, on behalf of each beneficiary of the said Trust
420 Gregg Avenue
P.O. Box 14
Reading, Pa. 19603

CUSTOMER CLAIM IN THE LIQUIDATION OF MORGAN, KENNEDY & CO., INC., AS OF MARCH 9, 1973

Change above if incorrect

Telephone: Area code 125 # 376-7103

Taxpayer Identification # or Social Security # :

1. Claim for money balances as of March 9, 1973:
   Morgan, Kennedy & Co., Inc. owes me (Credit (Cr.) balance) $ 133,236.15
   I owe Morgan, Kennedy & Co., Inc. (Debit (Dr.) balance) $ None

2. Claim for securities as of March 9, 1973: (please check answer)
   Morgan, Kennedy & Co., Inc. owes me securities Yes X No ___
   I owe Morgan, Kennedy & Co., Inc. securities Yes ___ No X
   If Yes, please list below (please attach additional sheets for more space if necessary):

Date of Transaction	Name of Security	Number of shares or par value bonds: Morgan, Kennedy & Co., Inc. owes me (Long)	I owe Morgan Kennedy & Co., Inc. (Short)
	(SEE ATTACHMENT)		

THE ABOVE CLAIM DOES NOT INCLUDE TRANSACTIONS AFTER MARCH 9, 1973.

3. Has there been any change in your account since March 9, 1973? Yes ___ No X
   If yes, please give details by attaching a separate sheet.
4. Are you related to any officer, director, employee, registered representative or person affiliated with Morgan, Kennedy & Co., Inc? Yes ___ No X
   If yes, specify relationship ___
5. Does anyone other than you or your spouse have a beneficial ownership in the above described account? Yes X No ___
   If yes, please identify by name and address such other person(s) and describe the extent of their ownership in a signed attachment to this claim.

(over)

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A10
Application of Eugene L. Bondy, Jr.

6. Are you an officer or director of Morgan, Kennedy & Co., Inc. or the beneficial owner of 5 per centum or more of any equity security (other than a non-convertible stock having fixed preferential dividend and liquidation rights) of that corporation? Yes ___ No X
   If yes, please explain in an attachment to this claim.
7. Have you ever filed a claim for securities or cash with any other trustee in a liquidation under the Securities Investor Protection Act of 1970? Yes ___ No X
   If yes, please furnish complete details in an attachment to this claim.
8. Have you authorized any person to execute transactions on your behalf on a discretionary basis for the above account? Yes ___ No X
   If yes, please furnish name of person _____

THE FOREGOING CLAIM IS TRUE AND ACCURATE:

DATE:	SIGNATURES:	
6/21/73		Trustee
6/21/73		Trustee
6/21/73		Trustee

(If account is carried in more than one name, all must sign. If other than a personal account, please state your capacity and authority)

"Whoever knowingly and fraudulently presents any false claim for proof against the estate of a bankrupt or uses any such claim in any bankruptcy proceeding ... shall be fined not more than $5,000 or imprisoned not more than five years, or both."
18 U.S.C. § 152

A legible copy of the following documentation should be forwarded to the trustee to support your claim and assist in its processing:

a. last customer statement received, together with your comments on differences, if any
b. a schedule describing how you determined the money balances and securities shown above
c. purchase and sales confirmations covering the items shown above
d. any other documentation which you believe would be of assistance in processing your claim such as cancelled checks, correspondence. receipts, etc.

This claim, together with supporting documentation, should be mailed promptly to:

Eugene L. Bondy, Jr., Trustee in the Liquidation of
Morgan, Kennedy & Co.,Inc.
P.O. Box 5796
Grand Central Station
New York, N.Y. 10017

EXHIBIT C

MORGAN, KENNEDY & CO., INC.

CUSTOMER CLAIMS OF

IRVING SUKNOW, HERBERT OSTROFF, AND DORIS RAUENZAHN ("TRUSTEES") TRUSTEES FOR THE READING BODY WORKS, INC. PROFIT SHARING PLAN TRUST ON BEHALF OF EACH BENEFICIARY OF THE SAID TRUST

ATTACHMENT

I. *Summary of Claim*

The Trustees are making this claim on behalf of each of the beneficiaries of the Trust, numbering approximately 108 individuals. The Trustees assert that each beneficiary is a separate customer of Morgan, Kennedy & Co., Inc. ("Morgan") under the Securities Investors Protection Act of 1970 ('the Act"). The Trustees are acting as such pursuant to an agreement dated April 12, 1957, between them and Reading Body Works, Inc., a Pennsylvania corporation.

The claim includes the right to 200 shares of Hoffman Electronics which were delivered to Morgan solely for the purpose of registration.

The Claim also includes the rights of the Trustees and their beneficiaries relating to a series of transactions in which Morgan effected sales transactions of securities of the Trust and accepted the securities, but failed to complete the sales. The net proceeds of such sales totalled $83,051.15. No part of such proceeds were ever paid to the Trust. The Trustees understand that Morgan diverted certain of the Trust's securities by pledging them for debts of Morgan instead of using them to complete the sales. The Trustees never authorized Morgan to hypothe-

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cate securities of the Trust. If any such securities are still in the possession of any such pledgee and if they should be returned to Morgan, they will become specifically identifiable securities of the Trust.

To the extent such securities may not be specifically identifiable, the Trust has a securities claim for them with respect to each beneficiary of the Trust.

To the extent that any such securities, or other securities traceable to them, are in the possession of Morgan, they are specifically identifiable securities of the Trust. If they are not specifically identifiable, the Trust has a securities claim for them with respect to each beneficiary of the Trust.

To the extent that Trust does not have a securities claim with respect to any such securities, it has a cash claim for the net proceeds of ther sale.

The claim also includes the right to a $50,000 U.S. Treasury Bill which Morgan purchased with the Trust's free credit balance funds. Morgan never delivered the Bill to the Trust. Instead, Morgan, without authorization, delivered the Bill to a bank as security for Morgan's debt to such Bank.

To the extent the Treasury Bill comes into the possession of Morgan, it will be a specifically identifiable security which belongs to the Trust.

If the Treasury Bill is not a specifically identifiable security, the Trust has a securities claim with respect to the Treasury Bill.

To the extent the Trust does not have a securities claim with respect to the Treasury Bill, it has a cash claim for its value at its maturity.

II. *Hoffman Electronics*

On or about October 5, 1972, the Trust purchased 200 shares of Hoffman Electronics Corp through Monaghan

& Company, Inc. ("Monaghan"), which carried them in street name. On or about February 8, 1973, Monaghan delivered the Certificate for such shares, No. NY/U-2668, to the Trust. On or about February 14, 1973, the Trust delivered the certificate to Morgan for re-registration in the name of the Trust. The Trust has never received a certificate in its name, nor the return of the certificate it delivered to Morgan.

Atttached hereto are true copies of:

1. Monaghan's purchase advice, October 5, 1972.
2. Monaghan's letter of transmittal
3. Monaghan's statement, December 31, 1972.
4. Morgan's receipt for the certificate

III. *U.S. Treasury Bill*

On or about January 31, 1973, Morgan purchased for the Trust, with the Trust's free credit balance funds, a 5.40% U.S. Treasury Bill, CUSIP #912793-QH-2, due March 1, 1973. The Trust never received the Bill from Morgan. Instead, Morgan delivered the Bill to Chemical Bank in connection with the indebtedness of Morgan to such Bank. Morgan had no right to do so. Attached hereto is a true copy of Morgan's purchase advice dated January 31, 1973.

IV. *Other Securities*

1. *AT&T Convertible $4.00 Preferred.* On or about February 13, 1973, the Trust sold through Morgan 400 shares of convertible $4.00 preferred stock of American Telephone & Telegraph Company. The net proceeds of the sale were to have been $24,097.41. Thereafter, the Trust delivered to Morgan AT&T's certificates 2201-8836 for 200 shares and 2907-6089 for 200 shares, solely for the pur-

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pose of completing the sale. Instead, Morgan, without any right to do so, delivered the certificates to Chemical Bank, apparently in connection with debt which Morgan owed to that Bank. The Trust has never received any of the proceeds of the sale. Attached hereto is a true copy of Morgan's sale advice dated February 13, 1973.

2. *AT&T Debenture, 7%, '01.* On or about February 13, 1973, the Trust sold through Morgan a $10,000 debenture, 7% 2/15/2001 of American Telephone & Telegraph Company. The net proceeds of the sale were to have been $9,627.92. Thereafter, the Trust delivered to Morgan AT&T's debenture No. R100347, solely for the purpose of completing the sale. Instead, Morgan, without any right to do so, delivered the debenture to Chemical Bank, apparently in connection with debt which Morgan owed to that Bank. The Trust has never received any of the proceeds of the sale. Attached hereto is a true copy of Morgan's sale advice dated February 13, 1973.

3. *AT&T Debenture, 8¾%, '00.* On or about February 13, 1973, the Trust sold through Morgan a $10,000 debenture, 8¾% 5/15/2000 of American Telephone & Telegraph Company. The net proceeds of the sale were to have been $11,170.83. The Trust delivered to Morgan AT&T's debenture No. 8117-2906, solely for the purpose of completing the sale. Instead, Morgan, without any right to do so, delivered the debenture to Chemical Bank, apparently in connection with Morgan's debt to that Bank. The Trust has never received any of the proceeds of the sale. Attached hereto is a true copy of Morgan's sale advice dated February 13, 1973.

4. *PT&T Stock.* On or about February 13, 1973, the Trust sold through Morgan 900 shares of Pacific Telephone & Telegraph stock. The net proceeds of the sale

were to have been $15,821.88. Thereafter, the Trust delivered to Morgan PT&T's certificates 71S-61613 and NB 183601-08, solely for the purpose of completing the sale. Instead, Morgan, without any right to do so, delivered the certificates to Chemical Bank, apparently in connection with debt which Morgan owed to that Bank. The Trust has never received any of the proceeds of the sale. Attached hereto is a true copy of Morgan's sale advice dated February 13, 1973.

5. *Anaconda Corp.* On or about February 8, 1973, the Trust sold through Morgan 300 shares of Anaconda Corp. stock. The net proceeds of the sale were to have been $6,351.82. Thereafter, the Trust delivered to Morgan, solely for the purpose of completing the sale, Anaconda's certificates N 56421 through N 564623 for 100 shares each. These certificates were cancelled by Anaconda's transfer agent on March 5, 1973, and new Anaconda certificates N 707401 through -03 for a like number of shares were issued to "Kenmorg," 5 Hanover Square, New York, New York. Instead of using the new certificates to complete the sale, Morgan delivered the new certificates to Chemical Bank, apparently in connection with Morgan's debt to that Bank. The Trust has never received any of the proceeds of the sale. The Trustees believe that Kenmorg is a nominee designation for Morgan, and that the shares, which belong to the Trust, are now registered in that name, the certificates being in the possession of Chemical Bank. Attached hereto are true copies of:

a. Morgan's sale confirmation dated February 8, 1973

b. Letter dated April 3, 1973 from First National City Bank, transfer agent for Anaconda.

6. *Itek Corporation.* On or about February 13, 1973, the Trust sold through Morgan 100 shares of Itek Corpora-

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ton stock. The net proceeds of the sale were to have been $4,331.31. Thereafter the Trust delivered to Morgan, solely for the purpose of completing the sale, Itek's certificate BC 19399. This certificate was cancelled by Itek's transfer agent and a new Itek certificate 21851 for a like number of shares was issued on March 8, 1973 to "Kenmorg," 5 Hanover Square, New York, New York. Instead of using the new certificate to complete the sale, Morgan delivered the new certificate to Chemical Bank, apparently in connecton with Morgan's debt to that Bank. The Trust has never received any of the proceeds of the sale. The Trustees believe that Kenmorg is a nominee designation for Morgan, and that the shares, which belong to the Trust, are now registered in that name, the certificates being in the possession of Chemical Bank. Attached hereto are true copies of:

a. Morgan's sale confirmation dated February 13, 1973

b. Lettter dated April 2, 1973 from The First National Bank of Boston, transfer agent for Itek.

7. *Syntex Corp.* On or about December 29, 1972, the Trust sold through Morgan 100 shares of Syntex Corp. stock. The net proceeds of the sale were to have been $8,234.83. Thereafter, the Trust delivered to Morgan Syntex's certificate JC 106718, solely for the purpose of completing the sale. The Trust has never received any part of the proceeds of the sale. The certificate the Trust delivered to Morgan was cancelled by Syntex's transfer agent on February 21, 1973, and new Syntex certificates, 457430/1, were issued to "Kenmorg," 5 Hanover Square, New York, New York. Attached hereto are true copies of:

a. Morgan's sale confirmation dated December 29, 1972.

b. Letter dated May 2, 1973, from the Chase Manhattan Bank, transfer agent for Syntex.

c. Letter dated June 1, 1973 from the Chase Manhattan Bank, transfer agent for Syntex.

8. *Colorado Bancorp.* On or about February 13, 1973, the Trust sold through Morgan 500 shares of Commercial Bancorporation of Colorado stock. The net proceeds of the sale were to have been $3,413.25. Thereafter, the Trust delivered to Morgan Colorado Bancorp.'s certificates AC 1887 through AC 1891, solely for the purpose of completing the sale. The Trust has never received any of the proceeds of the sale. The certificates the Trust delivered to Morgan were cancelled by Colorado Bancorp.'s transfer agent on March 2, 1973, and Colorado Bancorp.'s certificates AC 2020, AC 2022 and AC 2023, for 100 shares each, were issued to "Kenmorg," 5 Hanover Square, New York, New York. Other certificates were issued for the other 200 shares, being AC 2021 and AC 2019 or AC 2024, those shares being transferred out of Kenmorg on March 21, 1973. Attached hereto are true copies of:

a. Morgan's sales confirmation dated February 13, 1973.

b. Letter dated March 13, 1973 from Provident National Bank, transfer agent for Colorado Bancorp.

c. Letter dated April 19, 1973 from Provident National Bank, transfer agent for Colorado Bancorp.

V. *Cash Reconciliation*

Attached hereto is a summary of the transactions between Morgan and the Trust which show a computation of the cash debt of $133,236.15.

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VI. *Identification of Beneficiaries*

As of Mar. 9, 1973, the Reading Body Works, Inc. Profit Sharing Plan Trust had approximately 108 beneficiaries. Their names, their positions at Reading Body Works, Inc., and the percentage allocated at that time to each of them, is shown on a schedule attached.

VII. *Reservation of Rights*

The filing of this claim is not intended to, and shall not operate so as to effect any waver, impairment, or delay in the rights of the Trustees to proceed against parties other than Morgan with respect to the rights of the Trust described herein.

/s/ IRVING SUKNOW
Irving Suknow

/s/ DORIS RAUENZAHN
Doris Rauenzahn

/s/ HERBERT OSTROFF
Herbert Ostroff

(Attachments referred to in this Exhibit have been omitted in printing.)

EXHIBIT F

SECURITIES INVESTOR PROTECTION CORPORATION
TRUSTEE'S REQUEST FOR SIPC ADVANCE PAYMENTS TO CUSTOMERS
(based on claims determined as of Filing Date in the manner provided in the Act of 1970)

Request No. 22
Date May 17, 1974

Debtor — Morgan, Kennedy & Co., Inc.
Eugene L. Bondy, Jr., As Trustee

Address — Rogers & Wells
200 Park Avenue, New York, N.Y. 10017

Mailing address for funds requested _____

(Check will be made payable to the Trustee for the debtor.)

Note: Before making payments to customers from SIPC advances, the Trustee must obtain court authorization.

Number of attached pages: 1
(SIPC Form 11-1)

Advance requested for:	
Credit balances	$133,051.15
Cash in lieu of securities	
Total	$133,051.15

This request for advance is appropriate and necessary as provided for by the Securities Investor Protection Act of 1970.

/s/ EUGENE L. BONDY, JR. — Signature—Trustee — 5/17/74 Date

/s/ ROBERTA S. KARMEL — Signature—Attorney — 5/17/74 Date

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SIPC Form 11-1 (1 REV 3/71) SECURITIES INVESTOR PROTECTION CORPORATION 23RD DIST. Page 1 of ___ pages
Date ___

Trustee's report of proposed distributions to customers, excluding specifically identifiable property distributable to "cash customers",
and Request for SIPC Advance for Payments to Customers (based on claims determined as of Filing Date in the manner provided for in the Act of 1970)

In the matter of MORGAN KIMBERLY & CO., INC.

Claim No.	Customer name and address	Securities (Long)	(Short)	Description	Price	Value (Long)	(Short)	Net ledger cash balance Cr. [Dr.]	Net equity (C) Cash	Pro rata portion of securities available	Quantity	Value	Net equity to be distributed: Cash in lieu of securities	Quantity	Value	SIPC advance requested by Trustee: Cash credit balance	Total cash	Total net equity to be distributed	Balance of net equity: Securities value	Cash credit balance	Total
	FEES. REACTIVE RODY WORKS INC.																				
	C/O MELLROY, LEVINE, WEINBERG																				
	THE FIDELITY BLDG.							13315 15	13305 15	C						13315 15	13305 15				
	PHILADELPHIA, PA. 19109																				
	38-00662																				
																	13305 15	TOTAL FREE CREDIT			

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EXHIBIT I

SECURITIES INVESTOR PROTECTION CORPORATION
900 SEVENTEENTH STREET, N.W., SUITE 800
WASHINGTON, D.C. 20006 (202) 233-8400

June 28, 1974

Roberta S. Karmel, Esquire
Rogers & Wells
200 Park Avenue
New York, New York 10017

Re: Morgan Kennedy & Co., Inc.

Dear Roberta:

Mike Don informs me that the claim filed by the Trustees for Reading Body Works, Inc., Profit Sharing Plan Trust in the amount of $133,051.15 is not now approved for payment. Therefore, I am returning Request No. 22 dated May 17, 1974 requesting funds in the amount of $133,051.15, submitted per your letter of May 22.

In the last paragraph of your letter you ask us to forward $20,000.00 in the event that the entire $133,051.15 is not approved. I understand that a separate court order would be necessary before the $20,000.00 can be advanced.

Please resubmit request when the amount to be paid has been determined and approved.

Thank you for your cooperation.

Sincerely,

/s/ TOM
THOMAS R. CASSELLA
Manager—Operations

Application of Charles M. Solomon

(Caption omitted in printing)

Application for Order to Designate Claim of Trustees of Reading Body Works, Inc. Profit Sharing Plan

COMMONWEALTH OF PENNSYLVANIA
COUNTY OF PHILADELPHIA ss:

CHARLES M. SOLOMON, being duly sworn according to law, deposes and says:

1. He has read the sworn application of Eugene L. Bondy, Jr. executed September 5, 1974, and adopts herein paragraphs from that sworn application numbered 1, 4, 5, 6, 8, 9, 10, 12, 13, 14, 15, 16, 17, 18, 19 and 20.

2. This application is being made for an Order (the form of which is annexed hereto) as follows:

(a) The claim of the Trustees of Reading Body Works, Inc. Profit Sharing Plan shall be deemed to be a cash claim in the amount of $59,598.18, and a claim for securities in the amount of $74,336.25; and

(b) SIPC be ordered to pay to the Trustees immediately the sum of $50,000.00 whether or not the interpretation of "customers" is or is not resolved at this hearing; and

(c) Each of the 108 beneficiaries of the Trust be deemed a separate customer and therefore the claim should be paid in full by SIPC; or

(d) Each of the three Trustees be deemed a separate customer and therefore the claim of the Trust should be paid in full as a cash claim of $59,598.18 and as a claim for securities in the amount of $74,336.25.

3. Paragraph 7 of the Bondy application is revised herein to aver that during the months of December, 1972 and January and February of 1973, the Trustees author-

ized the Debtor to execute the sales of certain securities on behalf of the Trust. These securities were delivered to the Debtor with powers signed by the Trustees in order to complete these sales. Some of the sales were completed and credited to the Trustees' account by the Debtor. See Exhibit A attached hereto and made part hereof.

Other sales were not completed because the Debtor gave the securities with powers attached to Chemical Bank and before March 9, 1973, the filing date of this liquidation proceeding, these securities had been seized by Chemical Bank as collateral for the indebtedness from the Debtor to Chemical Bank. See Exhibit B attached hereto and made part hereof.

Although these sales were never completed, the net proceeds were credited to the account of the Trustees by the Debtor. Efforts by the Trustees to recover securities held by Chemical Bank have resulted in litigation in the United States District Court of the Eastern District of Pennsylvania and that litigation is presently pending.

4. Paragraph 11 of the Bondy application is revised herein to aver that by letter dated June 26, 1973, counsel for the Trustees made formal claim upon the Debtor on behalf of each of the beneficiaries of the Trust. The claim (a copy of which was annexed to the Bondy application as Exhibit B) dated June 20, 1973, made claim in the alternative for money balances of $133,236.15 and for securities as described in the attachment thereto (a copy of which was annexed to the Bondy application as Exhibit C). The footnote in the Bondy application in paragraph 11 is adopted.

Dated: Philadelphia, Pennsylvania
October 14, 1974

/s/ CHARLES M. SOLOMON
Charles M. Solomon

(Subscription omitted in printing)

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EXHIBIT "A"

Trade Date	Settlement Date	Present Location	Description	Net Proceeds
12/29/72	1/ 8/73	Sold	100 Snytex Corp.	$ 8,234.83
1/31/73	3/ 2/73	Redeemed	$50,000 Treasury Bill	50,000.00
2/13/73	2/21/73	Sold	200 Commercial Bancorp.	1,363.35
			Total cash claim	$59,598.18

Application of Charles M. Solomon

EXHIBIT "B"

Trade Date	Settlement Date	Present Location	Description	Net Proceeds	Gross Proceeds
2/ 8/73	2/16/73	CB	300 Anaconda Co.	$ 6,351.82	$ 6,450.00
2/13/73	2/21/73	Sold By CB	300 Commercial Bancorp.	2,049.90	2,100.00
2/13/73	2/21/73	CB	100 Itek	4,333.31	4,400.00
2/13/73	2/21/73	CB	900 Pac. Tel. & Tel.	15,821.88	16,087.50
2/13/73	2/21/73	CB	400 ATT $4 conv., pfd.	24,097.41	24,350.00
2/13/73	2/21/73	CB	$10,000 ATT 7% deb.	9,627.92	9,666.25
			Int. to 2/21/73		11.67
2/13/73	2/21/73	CB	$10,000 ATT 8.75% deb.	11,170.83	11,037.50
			Int. to 2/21/73		$233.33
			Total securities claim, excluding deductions for commissions and taxes		$74,336.25

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MEMORANDUM OPINION

ROY BABITT, *Bankruptcy Judge:*

Eugene V. Bondy, Jr., as trustee for the liquidation of the stock brokerage business of Morgan, Kennedy & Co., Inc. has petitioned this court for an order declaring that the single claim filed by the Trustee of the Reading Body Works, Inc., Profit Sharing Plan Trust for $133,051.15 be considered for distribution purposes as separate claims of the 108 beneficiaries of that profit-sharing trust and that, therefore, the liquidating trustee pay this claim in full under the scheme of the relevant statute. Morgan, Kennedy is presently in liquidation under the statutory scheme provided by the Securities Investor Protection Act of 1970, 15 U.S.C. §§78aaa, et seq. (SIPA).

The following undisputed facts set the stage for the controversy:

Pursuant to the terms of a profit-sharing plan adopted in 1957, Reading Body Works, Inc. (the "Company") established its trust for the benefit of its employees. The trust fund was administered by independent trustees and was maintained by yearly contributions made by the Company based upon its net earnings. Employees accumulated percentage interests in the fund based on their annual compensation level and consecutive years of service. Separate "accounts" were maintained for each employee in which he had a non-forfeitable vested interest subject to certain conditions pitched to termination of employment with the Company. Credit entries were made to each "account" according to the employee's proportionate share of the Company's yearly contribution and any increase in the market value of the fund.

On March 13, 1973, it was determined that the customers of Morgan Kennedy were in need of the protection afforded by the 1970 "SIPA" and Eugene L. Bondy, Jr. became the trustee for the liquidation of Morgan Kennedy's business. In accordance with the scheme of that statute, a claim by the profit-sharing trust was filed in the sum of $133,015.15,* the amount owed by Morgan Kennedy to the Trust on the relevant date of the proceedings to liquidate.

By letter dated October 9, 1973, Morgan Kennedy's trustee informed the Corporation created by SIPA to administer the Act (SIPC), 15 U.S.C. §78ccc, that he intended to treat each of the 108 beneficiaries of the profit-sharing trust as a separate "customer" for purposes of the recovery limit provided in Section 6(f) of the SIPA, 15 U.S.C. §§78fff(f)(1). He, therefore, requested that SIPC advance the full amount of the claims of the individual beneficiaries.

SIPC, however, informed Morgan Kennedy's trustee by letters dated May 23, 1974 and June 10, 1974 that it did not consider each beneficiary as a separate "customer" but felt that the profit-sharing trust itself was a single entity "customer" within the meaning of SIPA. From this SIPC concluded that it would therefore advance only a maximum of $20,000 as called for by the SIPA.

The issue thus presented is whether each of the 108 beneficiaries is a separate "customer" within the meaning of Section 6(f) of the SIPA, 15 U.S.C. §§78fff(f)(1). After carefully considering the legislative policy behind the creation of the SIPA it is my conclusion that the purpose of the Act is satisfied by treating each beneficiary of

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* The amount and validity of this claim as a claim is not contested in this proceeding. What is in controversy is the reach of the estate's exposure because of the nature of the trust and its beneficiaries.

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the trust as a separate "customer" and therefore entitled to the full coverage afforded.[1]

The SIPA and SIPC were created by Congress to provide investors with insurance against the loss of securities and cash left broker-dealers who thereafter encounter severe financial difficulties and must be liquidated. *U. S. Code Congressional and Administrative News*, 91st Cong., 2d Sess. 1970, p. 5255. Accordingly, the SIPA provides that the SIPC:

> ". . . shall advance to the trustee such moneys as may be required to pay or otherwise satisfy claims in full of each customer, but not to exceed $50,000 for *such customer*. . . ." Section 6(f)(1), 15 U.S.C. §78 fff(f)(1) [emphasis added].[2]

This controversy thus turns on the construction of the word "customer." The Act defines "customers" as:

> ". . . persons (including persons with whom the debtor deals as principal or agent) who have claims on account of securities received, acquired, or held by the debtor from or for the account of such persons. . . ."

Since Congress, in enacting the SIPA, meant to protect innocent investors, I have no doubt that the word "customer" should be read to include the individual bene-

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1. Since I have concluded that each of the 108 beneficiaries is a "customer" within the meaning of the SIPA there is no need to reach the alternative argument by the trustee that the claim is partially for securities and thus the statutory limit of $50,000 based on a claim of securities should be applicable.

2. In this case, $20,000 since only claims for cash are involved. See Section 6(f)(1)(A) and footnote (1) *supra*.

ficiaries of the profit-sharing trust. In effect, each beneficiary maintained his own account with Morgan Kennedy and it is quite irrelevant that books of this stockbroker carried the trust entity as the "owner" of the account or, for its own bookkeeping purposes, as its customer.

The Series 100 Rules adopted by the SIPC to provide guidelines for identifying accounts of "separate customers" of member stockbrokers clearly recognize that beneficial ownership of an account is the critical factor in determining who is to be considered a "customer" of a stockbroker member. Thus Rule 101(b) reads as follows:

> "An account held with a member by an agent or nominee for another person as a principal or beneficial owner shall, except as otherwise provided in the rules of this series, be deemed to be an individual account of such principal or beneficial owner."

Although under Subsection (c) of Rule 101 Morgan Kennedy's trustee could be required by the SIPC to provide satisfactory evidence as to the beneficial ownership of an account in the instant case, there is basically no dispute that the beneficial owners of the trust are the individual employees of the Company. I hold they must be deemed the real "customers" with respect to the account. Thus, each is entitled to the $20,000 maximum coverage.

The SIPC advances Rules 104 to support its contention that it is the profit-sharing trust entity and not the beneficiaries which is to be considered the customer to be protected by the Act. But Rule 104 does not specifically deal with this issue. Rather, Rule 104 deals with special instances where a beneficary or trustee *also* has an individual account with a broker-dealer subsequently liquidated pursuant to the provisions of the SIPA. Rule 104 does no more than apply the principle that accounts held

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in different capacities are to be considered accounts of "separate customers." In such instances the Rule provides such beneficiaries and trustees with double coverage for they are indeed separate customers. Rule 104 does not specifically treat the issue of separate coverage for the beneficiaries of a trust as a customer. Accordingly, reliance by the SIPC on Rule 104, apparently on the theory that it affords the only basis for separation of entities and no other is authorized, is misplaced.

It is also significant that the legislative history of the SIPA supports the reading of the statute that those within its reach, *i.e.*, securities investors, be provided with protection comparable to that afforded by the Federal Deposit Insurance Act ("FDIA") and the Federal Savings & Loan Insurance Act ("FSLIA"). See House Report No. 91-1613, Oct. 21, 1970, in *U. S. Code Congressional and Administrative News*, 91st Cong., 2d Sess. 1970, p. 5255, where it is said that

> "the need is similar, in many respects, to that which prompted the establishment of the Federal Deposit Insurance Corporation and the Federal Savings & Loan Insurance Corporation."

Under regulations adopted by the FDIC and the FSLIC each beneficiary of a trust which maintains an account at an insured institution is deemed a "separate customer" and is therefore individually entitled to protection up to the prescribed maximum. 12 C.F.R. §330—Appendix (1973). Since neither the SIPA or the Series 100 Rules provide any specific guidance in this area and in view of the Congressional expression to provide similar coverage under the SIPA as to that provided by the FDIA and the FSLIA, the regulations of the latter provided, at the very least, a strong indication as to how separate trust interests ought to be treated under the 1970 SIPA.

It is my conclusion that each of the 108 beneficiaries should be considered a separate "customer" within the meaning of Section 6(f)(1) of SIPA, 15 U.S.C. 78fff(f)(1). In so deciding I am not unmindful of the deference normally paid to the reading given by an agency charged with applying a statute. However, any deference in overriding the SIPC's construction (opposed to that of its trustee) must be overcome where the language of the statute does not support such construction and SIPC's own rules and the legislative history suggest otherwise.

Submit an order.

Dated: New York, New York
January 21, 1975.

/s/ Roy Babitt
Bankruptcy Judge

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Order of Judgment of Bankruptcy Judge Babitt

(Caption Omitted in Printing)

ORDER OF JUDGMENT

(Filed Feb. 14, 1975, Roy Babitt, Bankruptcy Judge)

Upon the application of Eugene L. Bondy, Jr., Esq., Trustee in the above-captioned matter ("Trustee"), to designate The Claim of the Trustees of the Reading Body Works Profit Sharing Plan Trust (the "Trust") as the separate claims of the 108 beneficiaries of the Trust and to declare that each such beneficiary is entitled to protection as a separate "customer" under Section 6(c)(2)(A)(ii) of the Securities Investor Protector Act, the application filed in opposition by the Securities Investor Protection Corporation, the application filed in support by the Trust and all other papers and proceedings herein, upon the memorandum opinion of this Court dated January 21, 1975, the Court having considered such submissions, and the Court having duly advised in the premises, it is

ORDERED that the claim filed by the Trustees of the Trust be and hereby is designated the separate claims of the 108 beneficiaries of the Trust and it is hereby declared that each such beneficiary is entitled to protection as a separate "customer" under Section 6(c)(2)(A)(ii) of the Securities Investor Protection Act.

Dated: New York, New York, February 14, 1975.

/s/ ROY BABITT
Bankruptcy Judge

Memorandum Order of District Judge Marvin E. Frankel

(Caption Omitted in Printing)

MEMORANDUM

FRANKEL, D. J.

The facts are undisputed and are outlined with characteristic lucidity by Bankruptcy Judge Babitt. The question is difficult. The statute, as a purely textual matter, favors the appellant. When the underlying policies and relevant analogies are considered, the balance tips the other way, as Judge Babitt held. Agreeing in the end with the ruling below, this court adds, or repeats, only a few observations:

1. While the statutory language on its face may favor SIPC, this must not be exaggerated. Even on this somewhat arid level, there is substantial room for debate. As SIPC stresses, the advances are provided for payments to "each customer. . . ." 15 U.S.C. §78fff(f)(1). But "customers" in turn are "persons . . . who have claims on account of securities . . . and . . . persons who have claims against the debtor arising out of sales or conversions of such securities. . . ." §78fff(c)(2)(A)(ii). It is scarcely an unbearable wrench to include employees for whom the Trust existed as such "persons." It is in this setting that the Bankruptcy Judge deemed significant SIPC's own Rule 101(b). For the purpose embraced by that Rule SIPC found itself comfortably able to look beyond the formalities of "title" and account designations to protect the "persons" affected with the kind of substantial interest Congress cared about. The analogy, if not decisive, is sound and useful.

2. Elsewhere in its own Rules SIPC has shown that there is no undeviating identity between an "account" and a "customer"; it has overridden the identity even where

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the result has been to diminish the protection for individual beneficiaries. SIPC's Rule 104(c) says that where more than one trust account is held for the same beneficiary "such accounts shall be combined so that the maximum protection afforded to such accounts in the aggregate shall be the maximum protection afforded to one 'separate customer' of the member." Piercing the formal designation of "accounts" in that situation, SIPC has looked at the individual human "beneficiary" as the measure of the protection. That approach should not be shunned when it is favorable to the real party in interest—the true investor with his small but vital stake—and adopted only when it hurts. The overriding purpose remains after all to effect "the speedy return of most customer property." *Securities Investor Protection Corp. v. Barbour*, 43 U.S.L.W. 4630, 4631 (May 19, 1975).

3. Acknowledging the consonance of the decision below with the Congressional purpose to afford maximum protection to the preponderant majority of small investors, SIPC nevertheless foretells disasters from Judge Babitt's ruling, extending even to threats of moment affecting the Treasury of the United States. The worry seems excessive. To be sure, the $100,000 or so affected by this case is not *de minimis*. And there will presumably be other cases and more money. But there is no concrete suggestion as to how catastrophes will happen. SIPC itself observes that there was an apparent desire in the Congress to cover fully by the $50,000 and $20,000 figures the "vast majority" of investors, well in excess of 90%. Hearings on H.R. 13308, H.R. 17585, H.R. 18081, H.R. 18109, H.R. 18458 Before the Subcomm. on Commerce & Finance of the House Comm. on Interstate & Foreign Commerce, 91st Cong., 2d Sess. 379-80 (1970). We are not directed to any actuarial surprise, any concrete projection,

or, certainly, any remote ground of policy for shuddering over the result herein approved.

4. We have been taught before now, at SIPC's urging, that the dryly literal definition of "customer" does not suffice to defeat "the patent legislative purposes." *S.E.C. v. F. O. Baroff Company, Inc.*, 497 F.2d 280, 282 (2d Cir. 1974). Though the cited case is not in point today, its familiar principle supports the result ordered by Judge Babitt. Forgetting its own employment of the principle, SIPC leans on language saying a customer must literally be one "with whom the debtor deals," 15 U.S.C. §78fff (c)(2)(iii), and one who is the addressee of notice that a proceeding has been commenced, §78fff(e).* That this proves too much is shown by referring again to SIPC's Rules.

The order of the Bankruptcy Judge is affirmed.
So ordered.

Dated, New York, New York, June 10, 1975.

/s/ MARVIN E. FRANKEL
U.S.D.J.

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* Brief of Appellant 23-24.

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Before:

MOORE and TIMBERS, *Circuit Judges*,
and COFFRIN,* *District Judge*.

Appeal from a decision of the United States District Court for the Southern District of New York, Marvin E. Frankel, *Judge*, affirming an order of Bankruptcy Judge Roy Babitt, which adjudged the one hundred and eight employee-beneficiaries of a trust created under a profit-sharing plan to be "customers" of a bankrupt stock brokerage house within the meaning of the Securities Investor Protection Act.

Reversed and remanded.

WILFRED R. CARON, Associate General Counsel, Washington, D. C. (Securities Investor Protection Corporation, Theodore H. Focht, General Counsel, Michael E. Don, Senior Attorney, of counsel), *for Applicant-Appellant*.

ROBERTA S. KARMEL, Esq., New York, N.Y. (Rogers & Wells, New York, N.Y., Laurence E. Cranch, of counsel), *for Defendants-Appellees*.

CHARLES M. SOLOMON, Philadelphia, Pa. (Fox, Rothschild, O'Brien & Frankel, Philadelphia, Pa., John C. McNamara, of counsel), *for Claimant-Appellee*.

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*Honorable Albert W. Coffrin, District Judge for the District of Vermont, sitting by designation.

MOORE, *Circuit Judge:*

In this appeal we are asked to determine whether the one hundred and eight employee-beneficiaries of a trust created under a profit-sharing plan qualify as "customers" of a bankrupt broker-dealer for the purpose of receiving compensation for losses available to such customers under the Securities Investor Protection Act of 1970 (SIPA), 15 USC §78aaa *et seq.*[1] The question was resolved in the beneficiaries' favor below. For the reasons which follow, we reverse and remand to the Bankruptcy Court.

I. FACTUAL BACKGROUND

In 1957 Reading Body Works, Inc. (Reading) established a profit-sharing plan (the Plan), pursuant to which a trust fund was created and maintained through yearly employer contributions based upon Reading's net earnings. The Plan provided that employees would earn "credits" or a percentage interest in the fund according to annual compensation level and consecutive years of service. The employees' individual credit units were in proportion to the units of all employees, and were based upon the current value of the assets in the trust. Separate accounts for each employee were maintained in the records of the trust to reflect the individual employee's accumulated credits and the current value of each employee's account. Each employee's interest in the trust was vested and non-forfeitable, but payable only upon the employee's termination of employment with Reading.

Title to the trust assets was held by three trustees (the Trustees) who were responsible for the management of the trust and the investment of its assets. In 1972, an ac-

1. All citations to the statute herein are to the United States Code.

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count was established with Morgan-Kennedy & Co. (the debtor). The account was held in the Trustees' names; the names of the various employee-beneficiaries did not appear on the debtor's books or records. Control over investment decisions was exercised solely by the Trustees, who communicated regularly with the debtor with respect to all transactions.

Liquidation proceedings against the debtor were commenced under SIPA in 1973, and a trustee (Bondy) was appointed. The Plan's Trustees subsequently submitted a claim for $133,015.15, the amount owed by the debtor to the trust on the filing date of the liquidation proceedings. Bondy thereafter informed the Securities Investor Protection Corporation (SIPC), the corporation created under SIPA that advances funds to liquidating trustees in order to compensate for customer losses, that he intended to treat the one hundred and eight trust beneficiaries as separate customers of the debtor; this would entitle each of the one hundred and eight to SIPA's maximum insurance coverage per customer of $50,000 for securities and $20,000 for cash held by the debtor as of the date of commencement of liquidation proceedings.

Bondy's interpretation of the term "customer" was disputed by SIPC. SIPC claimed that the trust, and not each of its beneficiaries, was the debtor's customer under SIPA; accordingly, SIPC recognized only one valid insurance claim. The Trustees supported Bondy's position; they also argued alternatively that, if SIPC's position respecting the definition of customer was correct, then the three Trustees should be treated as separate customers, and the claims accorded the $50,000 maximum award for securities held by the debtor.

Both the Bankruptcy Court and the District Court ruled in favor of Bondy and the Trustees on the definitional issue and did not reach the alternative arguments raised by the Trustees.

II. The Statutory Setting

SIPA was enacted by Congress in 1970

> to afford protection to public customers in the event broker-dealers with whom they transact business encounter financial difficulties and are unable to satisfy their obligations to their public customers. *S.E.C.* v. *Alan F. Hughes, Inc.*, 461 F.2d 974, 977 (2d Cir. 1972).

To this end SIPA establishes a Securities Investor Protection Corporation, commonly known by the acronym "SIPC". SIPC is a non-profit membership organization, whose members include all brokers or dealers who are members of a national securities exchange or are otherwise registered as brokers or dealers under 15 USC §78o(b). Unless a broker or dealer falls within one of the exceptions (not relevant here) contained in §78ccc(a)(2)(b), membership in SIPC is mandated. The role of SIPC has been aptly described by one commentator:

> SIPC's main function is to step in to liquidate a broker or dealer when customers' assets are in danger, and to protect a customer up to a total amount of $50,000 represented by proven claims to cash and securities expected to be in the hands of the broker or dealer. But no more than $20,000 represented by claims to cash can be recovered under the protective plan of SIPC, though the claim to securities may exceed this limit.[2]

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2. Guttman, "Broker-Dealer Bankruptcies," 48 NYULR 887, 909 (November 1973; footnotes omitted) (hereinafter cited as "Broker-Dealer Bankruptcies"). The source of the funds available to satisfy such claims is the SIPC Fund established by SIPA §78ddd; the fund is primarily supported by assessments on members.

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The decision to advance monies in satisfaction of outstanding claims against a bankrupt broker-dealer turns on whether the claimant qualifies as a "customer" of the broker-dealer. The maximum award available turns on whether the customer's losses arise from cash, or from securities held by the debtor.[3] The pertinent definitional language states that

> *"customers" of a debtor means persons (including persons with whom the debtor deals as principal or agent) who have claims on account of securities received, acquired, or held by the debtor from or for the account of such persons (I) for safekeeping, or (II) with a view to sale, or (III) to cover consummated sales, or (IV) pursuant to purchases,* or (V) as collateral security, or (VI) by way of loans of securities by such persons to the debtor, and shall include persons who have claims against the debtor arising out of sales or conversion of such securities, and shall include any person who has deposited cash with the debtor for the purpose of purchasing securities, but shall not include any person to the extent that such person has a claim for property which by contract, agreement, or understanding, or by operation of law, is part of the capital of the debtor or is subordinated to the claims of creditors of the debtor . . .
>
> 15 U.S.C. §78fff (c)(2)(A)(ii) (emphasis added).

III. "Customer" Status of the Employee-Beneficiaries

The status of trust beneficiaries is not dealt with specifically in either the above-quoted section or elsewhere in the statute. However, both the relevant case law and our

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3. 15 U.S.C. §78fff, subhead (c)(2)(A)(ii) and (f)(1)(A).

own interpretation of the term persuade us that the trust beneficiaries before us cannot come within the term "customer", no matter how far that word is stretched in service to the equitable ends of SIPA.[4]

In *S.E.C.* v. *F.O. Baroff Company, Inc.*, 497 F.2d 280 (2d Cir. 1974), this Court held that a voluntary lender of securities to a failing brokerage house, who made his loan to solely help out the company, was not a customer within the meaning of SIPA. The rationale for the Court's decision was that the lender could in no wise be considered a *public investor* of the broker-dealer, the essential criterion for establishing "customer" status under the language of SIPA and within the intent of Congress.

> The legislative history is clear that the 1970 Act was not designed to protect a lender in appellant's class. Most of the definition of "customers", including subpart VI, was taken from section 60e(1) of the Bankruptcy Act, 11 U.S.C. §96(e)(1), added in 1938, which established special rules "[w]here the bankrupt is a stockbroker." Both the legislative history of that provision and its use since enactment have stressed *protection to, and equality of treatment of, the public customer who has entrusted securities to a broker for*

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4. As appellants point out in their brief, br. at 24, this Court observed in *SEC v. Packer, Wilbur & Co.*, 498 F.2d 978, 983 (2d Cir. 1974) that

> "Arguments based solely on the equities are not, standing alone, persuasive. If equity were the criterion, most customers and creditors of Packer, Wilbur, the bankrupt, would be entitled to reimbursement for their losses. Experience, on the other hand, counsels that they will have to settle for much less. SIPA was not designed to provide full protection to all victims of a brokerage collapse."

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some purpose connected with participation in the securities markets.

The 1970 Act carries through the same theme. The House Report states: "The primary purpose of the reported bill is to provide protection for *investors* (emphasis supplied) if the broker-dealer with whom they are doing business encounters financial troubles." H.Rep.No. 91-1613, 91st Cong., 2d Sess. (1970), 3 U.S. Code Congressional and Administrative News, 91st Cong., 2d Sess., p. 5255 (1970). *Throughout the report "investors" is used synonymously with "customers", indicating that, in the eyes of Congress, the Act would protect capital markets by instilling confidence in securities traders.*

* * *

The emphasis throughout was on the customer as investor and trader . . . 497 F.2d at 282-3 (emphasis added; footnotes and citation omitted).

Emphasis on the customer as investor and purchaser/trader has been a consistent theme in cases in this Circuit. *See, e.g., S.E.C.* v. *Packer, Wilbur & Co.*, 498 F.2d 978, 984 (2d Cir. 1974); *S.E.C.* v. *Alan F. Hughes, Inc.*, 461 F.2d 974, 977 (2d Cir. 1972); *S.E.C.* v. *Kelly, Andrews & Bradley, Inc.*, 385 F.Supp. 948, 950 (S.D.N.Y. 1974); *S.E.C.* v. *Kenneth Bove & Co., Inc.*, 378 F.Supp. 697, 700; (S.D. N.Y. 1974).[5] Against this background, it is impossible to classify the Reading employees as "customers" of the

5. *Cf. Securities Investor Protection Corp. v. Barbour*, 95 S.Ct. 1733, 1736 (1975) wherein the Supreme Court, commenting on the impetus for the enactment of SIPA, implicitly acknowledged the predominance of the same attributes:

debtor.[6] The one hundred and eight beneficiaries were neither investors nor traders. The funds in the trust account came from Reading; the decision to entrust those funds to the debtor was the Trustees'. Appellees' counsel conceded at oral argument that none of the one hundred and eight would have had any standing as a "customer" of the then-solvent broker-dealer to give any buy or sell orders in the account. The financial relationship, insofar as the Plan is concerned, was entirely between the beneficiaries and their employer, *not* the broker-dealer. Moreover, with respect to the employees' participation in the Plan, we note that it amounted only to a bookkeeping matter on the Reading books. There could be an unlimited

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"Following a period of great expansion in the 1960s, the securities industry experienced a business contraction that led to the failure or instability of a significant number of brokerage firms. Customers of failed firms found *their cash and securities on deposit* either dissipated or tied up in lengthy bankruptcy proceedings. In addition to its disastrous effects on customer assets and investor confidence, this situation also threatened a "domino effect" involving otherwise solvent brokers that had substantial open transactions with firms that failed. Congress enacted the SIPA to arrest this process, restore *investor confidence* in the capital markets, and upgrade the financial responsibility requirements for registered brokers and dealers."
95 S.Ct. at 1736 (emphasis added).

6. The Trustees' further argument that the beneficiaries are entitled to recover as customers from SIPC since they are all "persons . . . who have claims on account of securities . . . held by the debtor from or for the account of such persons. . . ." (§78fff(c)(2)(A)(ii)) is belied by the very fact that the claimant before this Court is the trust, not the employees. Moreover, it is incorrect to describe the employees as possessing any claim which is presently reducible to a specific monetary sum. At most, the employees have an interest in the trust *res* which may be defeated under certain circumstances and which in any event is impossible of valuation until actual distribution is made.

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number of employee additions to, and subtractions from, the company's Profit Sharing Plan of which the broker would have no knowledge and with which no concern. The trust account itself was in the name of the Trustees who had the exclusive power to entrust the assets to the debtor, to invest and reinvest, and to purchase and trade securities in the account as they saw fit. In short, the single trust account, represented by the Trustees collectively, possessed the required attributes for customer status under SIPA; the Reading employees possessed none of those attributes.

Not only the relevant case law, but common sense as well, mandates this result. We are hard pressed to discern *any* of the usual traits of a customer relationship between the employee-beneficiaries and the debtor. Black's *Law Dictionary* (4th Ed., 1951) defines a "customer" as

> One who regularly or repeatedly makes purchases of, or has business dealings with, a tradesman or business house. Ordinarily, one who has had repeated business dealings with another. A buyer, purchaser, or patron. (citations omitted)

The employee-beneficiaries in the case before us made no purchases, transacted no business, and had no dealings whatsoever with the broker-dealer in question respecting the trust account. Indeed, they could not have any such dealings since the broker-dealer held no property belonging to any individual employee, in which such employee could trade or invest. Calculable amounts were payable to Reading's employees only in the event that, pursuant to the terms of the Plan, they became entitled thereto. The argument that, notwithstanding their complete anonymity and total incapacity to have dealings with the broker-debtor, the Reading employees were "customers" of Morgan-Kennedy stretches that term wholly beyond its limits.

Appellees point to provisions of the Federal Deposit Insurance Act (FDIA),[7] which provide insurance coverage to the beneficiaries of customer accounts, in urging that a similar result be reached here. We cannot accept appellees' analogy of the two statutes in the case at bar. SIPA and FDIA are independent statutory schemes, enacted to serve the unique needs of the banking and securities industries, respectively. The Congress recognized this when it rejected several early versions of the SIPA bill which were patterned on FDIA and which extended insurance coverage to certain beneficial interests represented by customer accounts.[8] Moreover, insofar as the definition of customer is concerned, this Court has held that its roots lie in Section 60(e) of the Bankruptcy Act,[9] a view which supports our interpretation of SIPA's definition of "customer".[10]

Both of the courts below relied heavily on SIPC's Series 100 Rules (the Rules), 3 CCH Fed. Sec. L.Rep. ¶26,667, to support the conclusion that all of the employee-bene-

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7. 12 U.S.C. §1811 *et seq.* The Federal Savings and Loan Insurance Act, 12 U.S.C. §1724 *et seq.*, contains similar provisions.

8. *See* S. 3988, S. 3989, S. 2348 and as amended, H.R. 13308, H.R. 17585.

9. 11 U.S.C. §1, *et seq.*

10. *S.E.C.* v. *F.O. Baroff*, *supra*, at pp. 1618-1619. *See, also*, *S.E.C.* v. *Kenneth Bove & Co., Inc.*, *supra*, at 378 F. Supp. 700, wherein the District Court commented:

> ". . . Undoubtedly, in framing the SIPA, Congress had in mind a similar concept of a protected customer, i.e., one who had entrusted his securities to the debtor and who was claiming against the debtor "on account of securities received, acquired, or held by the debtor". The definition in the Bankruptcy Act and SIPA sections is in identical language."

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ficiaries were customers of the debtor. This reliance was misplaced. The Rules set forth the circumstances under which accounts which are held by the same individual in different capacities shall be treated as the accounts of "separate customers"; the effect of treating the accounts in this fashion is to entitle each such account to the maximum protection available to a customer of the debtor. Only those accounts which are held by valid customers of the debtor can qualify for separate coverage.[11] Customer status under SIPA is therefore a prerequisite to the application of the Rules, and not a substitute therefor. Both of

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(Note 10 Continued)
Applicability of the Bankruptcy Act to liquidations under SIPA is specifically mandated by SIPA §78fff(c)(1):

> ". . . Except as inconsistent with the provisions of this chapter and except that in no event shall a plan of reorganization be formulated, a liquidation proceeding shall be conducted in accordance with, and as though it were being conducted under, the provisions of chapter X and such of the provisions (other than section 96(e) of Title 11) of chapters I to VII, inclusive, of the Bankruptcy Act as section 502 of Title 11 would make applicable if an order of the court had been entered directing that bankruptcy be proceeded with pursuant to the provisions of such chapters I to VII, inclusive. . . ."

Section 60(e)(1), which defines "customers of stockbrokers", is found in chapter VI of the Bankruptcy Act; accordingly, it is appropriate to look to that section for guidance here. *Cf. Exchange National Bank of Chicago v. Wyatt*, 517 F.2d 453, 458 (2d Cir. 1975). We note that, in interpreting §60(e) courts have applied the standard adopted by this Court in *S.E.C. v. F.O. Baroff*, *supra*. *See, S.E.C. v. First Securities of Chicago*, 507 F.2d 417, 420 (7th Cir. 1974).

11. Rule 100 reads in pertinent part:

Rule 100—General. (a) The rules set forth in this Series will be applied in SIPC in determining, for the purpose of Section 6(c)(2)(iv) and Section 6(f)(1) of the Act, what accounts held

the courts below engaged in an analysis of the Rules which took no cognizance of this fact.

We note further that the specific provisions of the Rules belie rather than support appellees' position. Under Rule 104 a qualifying trust account[12] may be afforded coverage as the account of a separate customer; however, in

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with a member SIPC (hereinafter called a "member") are to be deemed accounts of a "separate customer." . . .

(c) Accounts *held by a customer* in different capacities, as specified by the rules of this Series, shall be deemed to be accounts of "separate customers." For example, an account held with a member *by a customer* in his individual capacity and another account held by him as agent for another person shall be deemed to be accounts of "separate customers." No account *of a customer* with a member shall be deemed to be held in any capacity other than his individual capacity unless (1) the records of the member disclose such other capacity and contain satisfactory documentary evidence of the relationship on which such capacity is based, or (2) the Trustee appointed under Section 5(b)(3) of the Act (hereinafter called the "Trustee") provides SIPC with evidence satisfactory to it as to the existence and effectiveness of such relationship at the filing date. (emphasis supplied)

12. Rule 104 defines a "qualifying trust account" as follows:

(a) An account held with a member on behalf of a trust shall be deemed to be a 'qualifying trust account" if the records of the member disclose the name of the testator or settlor, the trustee of the trust and the names of the current beneficiaries of the trust and:

(i) the trust has been established by a will duly admitted to probate; or

(ii) the trust has been expressly established by a duly executed and delivered written instrument as an *inter vivos* trust under which the settlor

(1) may not at any time revoke the trust,

(2) is not a current beneficiary of the trust, and

(3) has no reversionary interest under the trust.

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no case may the *beneficiaries* of such a trust receive individual coverage as separate customers.[13] A similar result is reached by Rule 105 which provides that where co-owners of a qualifying joint account[14] also hold other accounts in different capacities, the joint account will be treated as

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(Note 12 Continued)
No account held on behalf of a "Totten" trust or any other revocable trust where, in the absence of revocation, the account will belong to a specified person on the death of the settlor shall be deemed to be a "qualifying trust account," nor shall any other account held on behalf of a trust that does not have an independent purpose be deemed to be a "qualifying trust account."

13. Rule 104 clearly states that the measure of protection is the single account, not its beneficiaries:

> (b) A qualifying trust account held with a member shall be deemed to be a "separate customer" of the member, distinct from the trustee, the testator or his estate, the settlor, or any beneficiary of the trust.
>
> (c) More than one qualifying trust account may be held with a member on behalf of a trust or trusts which were established by the same testator or settlor and have the same trustee, but where such accounts are held for the benefit of the same current beneficiary or beneficiaries, such accounts shall be combined so that the maximum protection afforded to such accounts in the aggregate shall be the maximum protection afforded to one "separate customer" of the member.

14. Subsection (b)(1) of Rule 105 defines qualifying joint account:

> A joint account shall be deemed to be a "qualifying joint account" if it is owned jointly, whether by the owners thereof as joint tenants with right of survivorship, as tenants by the entirety, or as tenants in common, or by husband and wife as community property, but only if each co-owner has executed a joint account agreement or similar agreement with the member and possesses authority to act with respect to the entire account.

belonging to a "separate customer"; maximum coverage available to a single customer only will be available to the joint account, and the co-owners will be required to divide the single award in proportion to their ownership interests in the account.[15] These provisions illustrate that, under SIPA, separate coverage for accounts held in different capacities is not to be confused with individual coverage for each individual owning some portion of, or interest in, the particular account. The former is explicitly provided for under the circumstances outlined in the Rules; the latter is as explicitly forbidden under the same Rules.

We find neither legislative nor judicial support for appellees' position, and we reject as inimical to our understanding of the term appellees' claim that the employee-beneficiaries of the trust account were customers of the broker-debtor.

IV. "Customer" Status of the Three Trustees

The Trustees have argued alternatively that, if SIPC's definition of a customer is to prevail, each of the three trustees must be considered a separate customer with separate claims against the debtor, based upon the debtor's dealings with each. This argument is without merit.

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15. The relevant provisions are found in Rule 105, §§(b)(2) and (3), (c) and (d):

> (2) Subject to paragraphs (c) and (d) of this rule, *each qualifying joint account with a member shall be deemed to be one "separate customer" of the member, and the protection afforded to the qualifying joint account as the account of a "separate customer" shall be made available to each co-owner in proportion to his interest in such joint account determined as provided in paragraph (a).*

Under SIPA, the protection afforded to customers of the debtor is limited.[16] The dollar maximums for advances

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(Note 15 Continued)

(3) Participation in a qualifying joint account shall not preclude any co-owner from being a "separate customer" by reason of an individual account with the member.

(c) All qualifying joint accounts with a member owned by the same combination of persons shall be combined so that the *maximum protection afforded to such accounts in the aggregate shall be the protection afforded to one "separate customer" of the member*, and shall be made available to each co-owner in proportion to his respective interests in the joint accounts determined as provided in paragraph (a).

(d) If a person participates in a qualifying joint account with a member which is not owned by the same combination of persons as own any other qualifying joint account with such member, *such joint account shall be deemed a "separate customer" of the member;* provided, however, that:

(i) *the protection afforded to such qualifying joint account shall be made available to each co-owner in proportion to his interest in that joint account determined as provided in paragraph (a);* and

(ii) without thereby increasing the protection afforded to any other co-owner, *the maximum protection afforded to any co-owner by reason of his total participation in qualifying joint accounts with a member shall be that of one "separate customer" of such member.*

(emphasis added)

16. 15 U.S.C. §78fff(f)(1) reads in pertinent part:

Advances for customers' claims.—In order to provide for prompt payment and satisfaction of the net equities of customers of debtor, SIPC shall advance to the trustee such moneys as may be required to pay or otherwise satisfy claims in full of each customer, but not to exceed $50,000 for such customer; except that—

(A) insofar as all or any portion of the net equity of a customer is a claim for cash, as distinct from securities, the

to customers under §78fff(f)(1) were selected by Congress with the intent of fully protecting the small investor only.[17] Accounts in excess of $50,000—which were estimated to comprise over 90% of the total dollar value of all accounts at the time SIPA was enacted[18]—were to be left unprotected to the extent of any loss in excess of the statutory maximum.[19]

Appellees concede that SIPA was designed to give maximum coverage to the small investor rather than to the large account. Bondy's br. at 10; Trustees' br. at 12. Nevertheless, the Trustees by their argument seek to evade this legislative scheme by attempting to secure for the trust account protection in excess of the $50,000 limit established under SIPA. Any suggestion that each of the three Trustees has a separate customer claim against the debtor is untenable. The Trustees together managed the account for the trust,[20] which was the true customer of the broker-

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amount advanced by reason of such claim to cash shall not exceed $20,000;

(B) a customer who holds accounts with the debtor in separate capacities shall be deemed to be a different customer in each capacity. . . .

17. *See*, Hearings on S.2348, S.2988, S.2989 before the Subcommittee on Securities of the Senate Committee on Banking and Currency, 91st Cong., 2d Sess., 1 (1970).

18. *See*, "Broker-Dealer Bankruptcies" at 909.

19. *See*, Hearings on H.R. 13308, H.R. 17585, H.R. 18081, H.R. 18109, H.R. 18458 before the Subcommittee on Commerce and Finance of the House Committee on Interstate and Foreign Commerce, 91st Cong., 2d Sess., 339-340 (1970).

20. We note in passing that the claimant-appellee in this suit identified itself as "Reading Body Works, Inc. Profit Sharing Trust", Reading's br. at 1, *not* as the Trustees of that trust.

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dealer;[21] the number of trustees sharing this responsibility was fortuitous.

If the available maximum of a SIPC advance depended upon the number of parties jointly holding an account, individuals could arbitrarily expand that figure at will. Such a result is obviously repugnant to the plain meaning of the statute and to the intent of Congress in passing it. Accordingly, we hold that the three trustees, by virtue of the trust account held by them collectively, may advance one customer claim only against the debtor.

V. Nature of the Trust's Claim Against the Debtor

The Trustees advanced a final argument before the Bankruptcy Court in the event that Judge Babitt ruled in favor of SIPC. The Trustees argued that their claim against the debtor was for securities as well as cash, thus entitling them to the $50,000 maximum advance available under SIPA for securities held by the debtor.[22] Both SIPC and Bondy disagreed, maintaining that the trust's claim was solely for a cash credit balance of $133,051.15. The parties' divergence of views arose from the fact that, following an order from the Trustees to sell certain securities, the debtor delivered certain of the securities to the Chemical Bank's Clearance Department, whereupon the bank refused to release them to purchasers and instead retained them to offset the debtor's loan obligations.

It was unnecessary for the Bankruptcy Court to reach this question since, under its holding, the trust's losses

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21. Reading's argument that SIPA's focus on "customers" and not "accounts" compels three recoveries for each of the Trustees therefore misses the point entirely, since the real customer was the Trust entity, and not the individuals charged with managing it.

22. 15 U.S.C. §78fff(f)(1)(A).

would be fully compensated irrespective of whether the $50,000 or $20,000 maximum were applied. Moreover, the issue appears to have received almost no attention before the Bankruptcy Court, the judge preferring to focus his attention on the status of the employee-beneficiaries.[23]

When the parties designated the record on appeal pursuant to Fed. R. App. P. 10 and Bankruptcy Rule 806, the only submission relative to this issue was the affidavit of William Ragusin, liquidator of the debtor, and accompanying exhibits thereto.[24] The District Court in its memorandum decision made no mention whatever of this issue. On appeal before this Court, the question received a minimum of attention by the parties. SIPC addressed itself to the nature of the trust's claim at the conclusion of its reply brief only. SIPC reply brief at 10-14. The Trustees devoted only brief space to the issue. Trustees' br. at 27-29. Bondy failed to discuss it entirely. In addition, there was some indication before the Bankruptcy Court that any determination regarding the nature of the trust's claim would require the resolution of certain factual issues.[25] Although

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23. See appellants appendix at p. 39a.

24. Appellee's Designation of Contents of Record, 73 Civ. 1057, March 7, 1975.

25. Ms. Karmel, counsel to the Trustee, stated to the Bankruptcy Judge that "[s]ome of the questions raised by the application of the claimant, the trustees for the Reading Body Works, do involve a determination as to certain factual issues, some of which are presently contained in the trustee's application and the cross-application of the trust, others of which I don't believe are really in dispute and could be provided in a further affidavit by the trustee or Mr. Raguson. However, it is the trustee's position that if the trustee's application is granted, these issues will all become moot. So, we would suggest that the Court not address itself to those further issues until it decides the trustee's application."

Proceedings before Judge (then Referee) Babitt, October 16, 1974, at 3-4.

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the Trustees and SIPC presented similar versions of the transactions in question to this Court, we cannot say, in light of the Bankruptcy Court proceedings and the sparseness of the parties' discussion, that the facts surrounding those transactions have been satisfactorily developed.

The Supreme Court has cautioned against the consideration, on review, of issues not reached by the lower court and not adequately presented in the reviewing tribunal. *Dandridge* v. *Williams*, 397 U.S. 471, 475 n.6, 90 S.Ct. 1153, 1157, 25 L.Ed. 2d 491 (1970); *Aetna Casualty & Surety Co.* v. *Flowers*, 330 U.S. 464, 468, 67 S.Ct. 798, 800, 91 L.Ed. 1024 (1947). Where, as here, there may be a need for findings of fact before a decision can be rendered, that caution takes on an added dimension. Accordingly, we decline to rule on the nature of the trust's claim until that issue has been fully aired and decided by the court below.

Reversed and remanded to the Bankruptcy Court for further proceedings consistent with this opinion.

Judgment

(Caption Omitted in Printing)

Appeal from the United States District Court for the SOUTHERN DISTRICT OF NEW YORK.

This cause came on to be heard on the transcript of record from the United States District Court for the SOUTHERN DISTRICT OF NEW YORK, and was argued by counsel.

ON CONSIDERATION WHEREOF, it is now hereby ordered, adjudged, and decreed that the order of said District Court be and it hereby is reversed and that the action be and it hereby is remanded to said district court for further proceedings consistent with the opinion of this court.

A. DANIEL FUSARO
Clerk

By VINCENT A. CARLIN
Chief Deputy Clerk

Several sections of the 1970 Act are involved on this Appeal. They provide, in pertinent part:

Section 6(a)
[General Purposes of Liquidation Proceedings]

"The purposes of any proceeding in which a Trustee has been appointed . . . shall be:

(1) As promptly as possible after such appointment, and in accordance with the provisions of this section—

(A) To return specifically identifiable property to the customers of the debtor entitled thereto;

(B) To distribute the single and separate fund, and (in advance thereof or concurrently therewith) pay to customers moneys advanced by SIPC, as provided in subsection (f) of this section;

(2) To operate the business of the debtor in order to complete open contractual commitments of the debtor pursuant to subsection (d) of this section;

(3) To enforce rights of subrogation as provided in this chapter; and

(4) To liquidate the business of the debtor.

Section 6(c)(2)(A)(ii)
[Customers]

"'customers' of a debtor means persons (including persons with whom the debtor deals as principal or agent) who have claims on account of securities received, acquired, or held by the debtor from or for the account of

such persons (I) for safekeeping, or (II) with a view to sale; or (III) to cover consummated sales, or (IV) pursuant to purchases, or (V) as collateral security, or (VI) by way of loans of securities by such persons to the debtor, and shall include persons who have claims against the debtor arising out of sales or conversions of such securities, and shall include any person who has deposited cash with the debtor for the purpose of purchasing securities, but shall not include any person to the extent that such person has a claim for property which by contract, agreement or understanding, or by operation of law, is part of the capital of the debtor or is subordinated to the claims of creditors of the debtor";

Section 6(c)(2)(A)(iv)
[Net Equity]

"'net equity' of a customer's account or accounts means the dollar amount thereof determined by giving effect to open contractual commitments completed as provided in subsection (d), by excluding any specifically identifiable property reclaimable by the customer, and by subtracting the indebtedness, if any, of the customer to the debtor from the sum which would have been owing by the debtor to the customer had the debtor liquidated, by sale or purchase on the filing date, all other securities and contractual commitments of the customer, and for purposes of this definition, accounts held by a customer in separate capacities shall be deemed to be accounts of separate customers";

Section 6(f)
[SIPC Advances to Trustee]

"(1) Advances for Customers' Claims.—In order to provide for prompt payment and satisfaction of the net

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equities of customers of debtor, SIPC shall advance to the trustee such moneys as may be required to pay or otherwise satisfy claims in full of each customer, but not to exceed $50,000 for such customer; except that

(A) insofar as all or any portion of the net equity of a customer is a claim for cash, as distinct from securities, the amount advanced by reason of such claim to cash shall not exceed $20,000;

(B) a customer who holds accounts with the debtor in separate capacities shall be deemed to be a different customer in each capacity";

* * *

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1975

No. 75-1524

TRUSTEES OF THE READING BODY WORKS, INC. PROFIT SHARING PLAN TRUST, *Petitioners*

v.

SECURITIES INVESTOR PROTECTION CORPORATION, ET AL., *Respondent*

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Second Circuit

BRIEF IN OPPOSITION OF RESPONDENT SECURITIES INVESTOR PROTECTION CORPORATION

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BRIEF IN OPPOSITION OF RESPONDENT SECURITIES INVESTOR PROTECTION CORPORATION

QUESTIONS PRESENTED

For purposes of a proceeding to liquidate the business of a broker-dealer under the Securities Investor Protection Act of 1970[1] (the "1970 Act"), the term "customers" of the broker-dealer is carefully defined in section 78fff(c)(2)(A)(ii)[2] which was de-

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[1] 15 U.S.C. § 78aaa *et seq.*

[2] All citations to sections of the 1970 Act will be to sections of Title 15 of the United States Code.

rived from section 60e(1) of the Bankruptcy Act.[3] The claim of each customer based on his securities account may be satisfied from the funds of respondent Securities Investor Protection Corporation ("SIPC") to a maximum of $50,000 if the broker-dealer's assets are insufficient to satisfy the claim.

The Petitioners' statement of the first "Question Presented" is imprecise. Respondent SIPC would state that question as follows:

> Whether by its definition of "customers" in the 1970 Act Congress intended to include all employees participating in an employer's profit sharing plan as the separate "customers" of the broker-dealer with respect to a securities account (i) which was opened, maintained and controlled exclusively by the three co-trustees of the trust created under the plan, (ii) over which the employees had no rights or control whatsoever, and (iii) title to the securities or cash in which was vested exclusively in the co-trustees as part of the trust *res*.

The Petitioners' statement of the second question is adequate.

The Petitioners' reference under "Questions Presented" to each employee as one "who maintained an account with the debtor" (Petition at 3) is erroneous and misleading.

JURISDICTION

The Petitioners invoke the jurisdiction of this Court under 28 U.S.C. § 1254(1). However, this being a controversy in bankruptcy the jurisdiction of this

[3] 11 U.S.C. § 96e(1).

Court is also primarily derived from 11 U.S.C. § 47(c).[4]

STATUTES INVOLVED

In addition to the basic definition of "customers" included in the Petitioners' Appendix, Section 78fff (c)(2)(A)(iii) of the 1970 Act provides:

> "'cash customer' means, with respect to any securities or cash, customers entitled to immediate possession of such securities or cash without the payment of any sum to the debtor, and for purposes of this clause, the same person may be a cash customer with reference to certain securities or cash and not a cash customer with reference to other securities or cash;"

The Petitioners' account owed no sum to this debtor.

STATEMENT OF THE CASE

This case arises in a proceeding for the liquidation of Morgan, Kennedy & Co., Inc. ("Debtor") under the 1970 Act. The Petitioners are the three Trustees of the Trust created under the Profit Sharing Plan ("Plan") established by Reading Body Works, Inc. ("Reading") for its employees ("Reading Employees"). The respondents are SIPC which

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[4] See Mitchell Store Building Co. v. Carroll, 232 U.S. 379 (1914). A liquidation proceeding under the 1970 Act is substantially governed by provisions of the Bankruptcy Act except to the extent they are inconsistent with the 1970 Act. See 78fff(c)(1). Insofar as it provides for liquidation proceedings, the 1970 Act is predominantly an exercise of the bankruptcy power of the Congress. Exchange National Bank of Chicago v. Wyatt, 517 F.2d 453, 459-460 (2d Cir. 1975). The *Wyatt* case holds that appeals to the Court of Appeals are governed by section 24a of the Bankruptcy Act, 11 U.S.C. § 47(a). See discussions *infra* at pages 7 *et seq.*, especially 11, n. 24; 18; —; n. 46, ll. 7-12.

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commenced the liquidation proceeding, and Eugene L. Bondy, Jr. who was appointed trustee for the liquidation of the Debtor's business.

The Plan was funded entirely by Reading's contributions to the Trust. Neither Reading nor Reading's Employees had any title to the assets of the Trust. Title was in the Trustees who were vested with the sole power to hold, invest and reinvest. The Trustees were empowered to act only upon concurrence of a majority.

Reading's Employees earned benefits based solely on service in Reading's employ.[5] Discharge for certain causes worked a forfeiture of all rights; otherwise, benefits became vested and non-forfeitable over a period of time,[6] and were payable on termination of employment. Payments of benefits to Reading's Employees were to be made by the Trustees upon the written order of the committee responsible under the Plan for its administration.

The Trust's account with the Debtor was opened by the Trustees in December, 1972. The account was held in the following name and style on the Debtor's records: "Trustees For Reading Body Works Profit Sharing Plan Dated April 12, 1957." Control over investment decisions was exercised solely by the Trustees. They communicated regularly with the Debtor with respect to all transactions.

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[5] Each of Reading's Employees was assigned "credit units" on each anniversary date of the Plan. A value was assigned to the "credit units" in the proportion they bore to the total "credit units" of all Reading's Employees, based on the value of the assets in the Trust.

[6] Increasing percentages of an employee's total "credit units" vested over a period of ten years.

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On the "filing date"[7] of this liquidation proceeding the books and records of the Debtor reflected a cash credit balance in the account of $133,051.15 for which the Trustees filed a claim. It does not appear from the record what percentage of total Trust assets was involved in this account.

REASONS FOR DENYING THE WRIT

I.

THE PETITIONERS HAVE FAILED TO DEMONSTRATE THAT THE QUESTIONS PRESENTED ARE "CERTWORTHY" WITHIN THE MEANING OF THIS COURT'S RULE 19 AND THE CRITERIA ESTABLISHED BY ITS DECISIONS, PARTICULARLY IN LIGHT OF THE INTERLOCUTORY NATURE OF THE JUDGMENT OF THE COURT OF APPEALS.

The judgment of the Court of Appeals is interlocutory.[8] Although the petition may be denied for that reason alone, at the very least the Petitioners' burden is more onerous than in cases involving a final

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[7] The "filing date", as defined in section 78eee(b)(4)(B), is the date as of which the securities and cash claims of customers are valued under section 78fff(c)(2)(A)(iv).

[8] Under the interpretation of the 1970 Act adopted by the Court of Appeals, whether and to what extent the claim of the Trust is for securities or cash is now a viable question materially affecting the amount of recovery (see page 14, *infra*). Hence the Court remanded the case for resolution of the remaining factual and legal issues. In contrast, those issues were mooted by the District Court's interpretation which would have afforded complete satisfaction of the Trust's claim irrespective of whether it is, in whole or part, a claim for securities. The Petition attempts to avoid the interlocutory character of the Court of Appeals' judgment by the unavailing comment that the issues of law and fact which were remanded have "nothing to do with the finality of the issue here involved." (Petition at 5) This observation confuses the principles of finality of judgment with the doctrine of "law of the case". See Hamilton-Brown Shoe Co. v. Wolf Brothers & Co., 240 U.S. 251, 258 (1916).

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judgment. *Brotherhood of Locomotive Firemen v. Bangor & Aroostook, R.R.*, 389 U.S. 327 (1967); *Hamilton-Brown Shoe Co. v. Wolf Brothers & Co.*, 240 U.S. 251, 258 (1916); *Mitchell Store Building Co. v. Carroll*, 232 U.S. 379 (1914) (bankruptcy); *American Construction Co. v. Jacksonville, T. & K. W. Ry.*, 148 U.S. 372, 384 (1893); R. STERN & E. GRESSMAN, SUPREME COURT PRACTICE § 4.19, at 180 (4th ed. 1969).

The Petitioners fail to demonstrate unusual circumstances sufficient to warrant review by this Court. The decision of the Court of Appeals is not in conflict with the decision of any other court. Indeed, it is so clearly the ineluctable result of sound analysis that it will undoubtedly command the respect of courts in other Circuits should the issue again arise. The Court of Appeals below has had extensive experience with the 1970 Act.[9] Although the questions presented are relatively important in the sense that most federal questions are important, there is no need that they be settled by this Court at this time.

Shorn of its curious rhetoric concerning an alleged conflict between the 1970 Act and other unrelated federal statutes,[10] the Petition is essentially a naked claim of error and a plea for judicial legislation.

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[9] See Exchange National Bank of Chicago v. Wyatt, 517 F.2d 453 (2d Cir. 1975); SIPC v. Charisma Securities Corp., 506 F.2d 1191 (2d Cir. 1974); SEC v. Packer, Wilbur & Co., Inc., 498 F.2d 978 (2d Cir. 1974); SEC v. F. O. Baroff Co., Inc., 497 F.2d 280 (2d Cir. 1974); SEC v. Oxford Securities, Ltd., 486 F.2d 1396 (2d Cir. 1973); SEC v. Alan F. Hughes, Inc., 481 F.2d 401 (2d Cir.), *cert. denied*, 414 U.S. 1092 (1973); SEC v. Alan F. Hughes, Inc., 461 F.2d 974 (2d Cir. 1972).

[10] The Petition refers to the Employee Retirement Income Security Act, the Federal Deposit Insurance Act, and the Federal Savings and Loan Insurance Act.

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Bereft of meaningful analysis of the provisions and legislative history of the 1970 Act or the antecedent provisions of section 60e of the Bankruptcy Act, the Petition merely urges this court to *imply* a remedy in order to produce the result it seeks (Petition at 10-15). This is hardly a case involving the doctrine of implied rights of action enunciated in the cases cited by Petitioners.[11] The 1970 Act meticulously provides for the rights of customers. The question is merely one of statutory construction, and the Petitioners have failed to show that the rationale and analysis of the Court of Appeals is anything but a cogent and irrefutable application of the 1970 Act as it was written and intended.

II.

THE COURT OF APPEALS WAS CLEARLY CORRECT IN DECIDING THAT THE TRUST, ON BEHALF OF WHICH THE TRUSTEES MAINTAINED A SINGLE ACCOUNT WITH THE DEBTOR, WAS THE "CUSTOMER" OF THE DEBTOR WITHIN THE MEANING AND INTENT OF THE 1970 ACT.

A liquidation proceeding under the 1970 Act is a practical equivalent to a stockbroker bankruptcy conducted in accordance with section 60e of the Bankruptcy Act, with the added feature of SIPC's funds as a supplemental source for the satisfaction of customers' claims against a debtor's estate (discussed *infra* at 14). Each customer (as defined) with a claim for the net equity of his account or accounts is entitled to a maximum of $50,000 protection from SIPC's funds.[12] The definitions of customer

[11] Petitioners cite Cort v. Ash, 422 U.S. 66 (1975); SIPC v. Barbour, 421 U.S. 412 (1975); and National Rail Passenger Corp. v. National Association of Rail Passengers, 414 U.S. 453 (1974).

[12] Section 78fff(f).

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and net equity are not the unique contrivances of the 1970 Act. They are derived (*in haec verba* for purposes of this issue) from section 60e of the Bankruptcy Act (discussed *infra* at 11-13).[13] Hence a brief analysis of section 60e and its genesis is essential.

History And Effect Of Section 60e Of The Bankruptcy Act

Prior to section 60e the common law of the several states largely determined the rights of margin and cash customers in stockbroker bankruptcy proceedings. Both were relegated to the status of general creditors if they could not trace their securities under contemporary tracing doctrines.[14] In the final analysis, various principles made the rights of margin and cash customers depend largely upon fortuitous circumstances affecting their ability to trace and reclaim their securities.[15] The law came under heavy criticism which led to the enactment of section 60e as part of the Chandler Act.[16]

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[13] See note 28, *infra;* see also SEC v. F. O. Baroff Co., Inc., 497 F.2d 280 (2d Cir. 1974); SEC v. Aberdeen Securities Co., Inc., 480 F.2d 1121 (3d Cir.), *cert. denied,* 414 U.S. 1111 (1973).

[14] An excellent discussion may be found in Smith, *Margin Stocks,* 35 HARV. L. REV. 485 (1922).

[15] A very helpful summary may be found in In re J. C. Wilson & Co., 252 Fed. 631 (S.D.N.Y. 1917).

[16] Hagar, *The Bankruptcy Law as Applied To Stockbrokerage Transactions,* 30 *Yale L. J.* 488 (1921); Note, *The Rights of a Customer in Collateral Security Given a Stockbroker,* 22 COL. L. REV. 155 (1922); Oppenheimer, *Rights and Obligations of Customers in Stockbrokerage Bankruptcies,* 37 HARV. L. REV. 860 (1924); McLaughlin, *Amendment of the Bankruptcy Act,* 40 HARV. L. REV. 341, 383-385 (1927); Holohan, *Contribution Among Securities Pledged by a Defaulting Stock Broker,* 4 SO. CAL. L. REV. 1 (1930); McLaughlin, *Aspects of the Chandler Bill to Amend the Bankruptcy Act,* 4 U. CHI. L. REV. 369 (1937).

Section 60e was intended to overcome the existing inequities which the law had visited upon conventional margin and cash customers. There was no intention, or need, to define "customers" in a unique or unorthodox manner. This is clear from the legislative history,[17] and has consistently been so understood by commentators[18] the SEC[19] and the courts.[20] Section 60e was intended for the benefit of margin and cash customers, as a class, who entrusted their securities to

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[17] H.R. Rep. No. 1409, 75th Cong., 1st Sess. 31 (1937); House Hearings on H.R. 6439, 8046 Before the House Comm. on the Judiciary, 75th Cong., 1st Sess. 125-131 (1937); Analysis of H.R. 12889, 74th Cong., 2d Sess. 192-93 (Comm. Print 1936).

[18] Weinstein, *The Bankruptcy Law of 1938*, 122 *et seq*, (1939) (hereinafter "Weinstein"); Gilchrist, *Stockbrokers' Bankruptcies: Problems Created by the Chandler Act*, 24 MINN. L. REV. 52 (1939); Comment, *The Bankrupt Stockbroker: Section 60e of the Chandler Act*, 39 COL. L. REV. 485 (1939). One commentator who was involved in the legislative process observed: "This new subdivision is intended to make the law uniform and to avoid inequities in distribution. Upon the bankruptcy of a stockholder, all margin and cash customers are treated as a single class and the securities and proceeds on hand for the purchase or from the sale of the securities of such customers are set up into a single and separate fund, to be distributed, except as otherwise provided in this subdivision, pro rata among such margin and cash customers, according to their respective net equities in their trading accounts." Weinstein, *supra* at 122.

[19] Report of Special Study of Securities Markets of the Securities and Exchange Commission, H. R. Doc. No. 95, Pt. 1, 88th Cong., 1st Sess. at 410 *et seq.*

[20] See, *e.g.*, Tepper v. Chichester, 285 F.2d 309 (9th Cir. 1960); Gordon v. Spalding, 268 F.2d 327 (5th Cir. 1959); In re McMillan, Rapp & Co., 123 F.2d 428 (3d Cir. 1941); SEC v. First Securities Co. of Chicago, 366 F. Supp. 367 (N.D. Ill. 1973), *rev'd on other grounds*, 507 F.2d 417 (7th Cir. 1974).

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their broker.[21] It contemplated transactions "in the form usual to dealings" between the customer and his broker and related only to securities held for the customer's account.[22]

Section 60e permitted limited tracing by customers. Thus, "cash customers" (as defined) were entitled to reclaim fully-paid securities which were their "specifically identifiable property" (as defined). To adjust the previous inequities, all other property (as defined) held by the stockbroker for customers was classified as a "single and separate fund" (as defined) for the benefit of all customers as a "single and separate class of creditors" (as defined). Each customer was entitled to his pro rata share of that fund based on the "net equity" (as defined) of his account. The terms customer and cash customer were defined in a manner consistent with common industry usage. The definition of customer was merely "designed to cover every form of transaction dealt with" under section 60e[23]—the customary activities in a typical securities account.

The 1970 Act

The background and general purposes of the 1970 Act are familiar to this Court. *SIPC v. Barbour*, 421 U.S. 412 (1975). Discussion will be confined to those provisions relevant to the questions presented.

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[21] See *e.g.*, SEC v. First Securities Co. of Chicago, 507 F.2d 417, 420-22 (7th Cir. 1974); In re Barraco and Co., 478 F.2d 517, 520 (10th Cir. 1973); Mardick v. Stover, 392 F.2d 561, 564 (9th Cir. 1968); Bush v. Masiello, 55 F.R.D. 72, 75 (S.D.N.Y. 1972).

[22] Cases cited note 20 *supra*, especially SEC v. First Securities Co. of Chicago, 507 F.2d at 421.

[23] Weinstein, *supra*, n. 18 at 123.

As noted above, a liquidation proceeding is essentially a section 60e bankruptcy [24] in which the debtor's assets are augmented by SIPC's funds within the limits of the statute. The decision to accomplish the broad objective of the 1970 Act by means of that vehicle was made after earlier approaches derived from the Federal Deposit Insurance Act were rejected as ill-suited to the securities industry.[25] As the cited portions of legislative history show, rejection of an FDIA approach largely resulted from the judgment and exhortation of both the SEC and the securities industry.[26]

Section 35(m)(10)(A) of the first bill jointly drafted by the SEC and the industry incorporated the section 60e definitions ("customer", "net equity" etc.) by reference.[27] With some minor modifications not here relevant (discussed *infra* at 12-13), the 1970 Act actually restated those definitions *in haec verba*. Congress explicitly stated its intention not to vary the meaning of the section 60e definitions. Thus, both the Senate and House Reports state:

> "In addition, the bill uses certain terms defined in section 60e *with the meanings there established*,

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[24] See, *e.g.*, Exchange National Bank of Chicago v. Wyatt, *supra*, n. 9; SEC v. Aberdeen Securities Co., Inc., *supra*, n. 13.

[25] Hearings on S. 2348, S. 2988, S.2989 Before the Subcommittee on Securities of the Senate Committee on Banking and Currency, 91st Cong., 2d Sess. 29, 175-77, 185, 191, 210-212, 255-257, 267-268 (1970) (hereinafter "Senate Hearings"); Hearings on H.R. 13308, H.R. 17585, H.R. 18081, H.R. 18109, H.R. 18458 Before the Subcommittee on Commerce and Finance of the House Comm. on Interstate and Foreign Commerce, 91st Cong., 2d Sess. 221-222 (1970) (hereinafter "House Hearings").

[26] One prominent industry representative observed: "Models chosen from one field of activity rarely fit exactly the needs of another field. I do not think the pattern of the FDIC fits the securities industry very well." Senate Hearings at 29.

[27] Senate Hearings at 261; House Hearings at 324.

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except as further defined in the bill". (emphasis added)[28]

It has been aptly stated that the 1970 Act was an ". . . engraftment of insurance provisions upon the preexisting Section 60(e) bankruptcy provisions applicable to stockbrokers, 11 U.S.C. § 96(e)."[29] Because sections 78fff(c)(2)(A)-(D) cover the definitions and other matters included in section 60e, section 78fff excludes section 60e from the operation of its terms which incorporate many provisions of the Bankruptcy Act.

In consequence of the foregoing, the rights of customers in a 1970 Act liquidation are tied to the section 60e concepts of customer, cash customer, specifically identifiable property, net equity and single and separate fund—"with the meanings there established." The definition of customers[30] conforms exactly to the definition in section 60e except for three changes not relevant here.[31] The definition of net

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[28] S. Rep. No. 91-1218, 91st Cong., 2d Sess. 10 (1970) (hereinafter "Senate Report"); H.R. Rep. No. 91-1613, 91st Cong., 2d Sess. 9 (1970) (hereinafter "House Report"); See also Senate Report at 13 and House Report at 10, 20.

[29] SEC v. Aberdeen Securities Co., Inc., *supra* n. 13 at 1123.

[30] Section 78fff(c)(2)(A)(ii).

[31] ***First***, it includes persons with transactions as to which the debtor acted as principal (dealer), thereby correcting an ambiguity in section 60e which led to the exclusion of such a person in Gordon v. Spalding, 268 F.2d 327 (5th Cir. 1959). See Senate Hearings at 261. ***Second***, it now specifically includes persons who had deposited cash for the purpose of purchasing securities, thereby resolving another ambiguity under section 60e. See Report of Special Study of Securities Markets of the Securities and Exchange Commission, H.R. Doc. No. 95, Pt. 1, 88th Cong., 1st Sess. 416 (1963). ***Third***, the definition now specifically excludes persons to the extent their claims relate to capital contributions or subordinated loans to the debtor.

equity [32] was likewise taken *in haec verba* from section 60e except for three changes, of which two are as follows.[33] While section 60e referred only to the "account" of a customer, the 1970 Act definition refers to the "account or accounts" of a customer. This was designed to limit the maximum protection to $50,000 per customer.[34] Correspondingly, language was added to assure separate protection to the same person acting "in separate capacities" with respect to different accounts. There is nothing whatever in the "customer" or "net equity" definitions in the 1970 Act to suggest that Congress meant to define customers so as to include persons other than the conventional cash or margin customers contemplated by section 60e.

Just as under section 60e, under section 78fff(c)(2)(B) customers are a single and separate preferred class of creditors who share pro rata in the single and separate fund, and then *pari passu* with general cred-

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[32] Section 78fff(c)(2)(A)(iv).

[33] The third gives effect to open contractual commitments completed as provided in section 78fff(d). That section authorizes the trustee to complete interbroker transactions with the use of SIPC's funds if necessary. This authority was designed to avoid the so-called "domino effect," namely, the chance that the debtor's demise might precipitate the failure of one or more other broker-dealers. House Report at 9; Senate Report at 4, 11; Senate Hearings at 147. See also SEC v. Packer, Wilbur & Co., Inc., *supra* n. 9. SEC v. Aberdeen Securities Co., Inc., *supra* note 13. Such transactions may involve a customer's account and must therefore be considered in calculating his "net equity". That was unnecessary under section 60e because the completion of such open transactions was not authorized.

[34] The $50,000 protection afforded by section 78fff(f)(1) is based on a customer's "net equity". Without this change in the "net equity" definition, each customer might have been deemed protected to $50,000 for each of his accounts.

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itors in the general estate. However, under section 78fff(f)(1) SIPC's funds are now available to cover deficiencies in the debtor's estate within prescribed limits (discussed below). Contrary to the Petitioners' suggestion (Petition at 9) the availability of those funds has no legitimate interpretive impact on the definitions of customer, net equity and other terms which establish the substantive rights of persons. It simply shores up the estate so that customers are no longer entirely dependent for their recoveries upon the debtor's assets.

Under section 78fff(f)(1) SIPC may advance a maximum of $50,000 to satisfy the net equity of each customer. Of that, only $20,000 may be advanced for that portion of the net equity which is based on a cash credit balance with the debtor, as distinct from securities positions. To the extent SIPC makes such advances it is subrogated to the rights of customers against the debtor's estate. The Petitioners' numerous references to conventional insurance are inappropriate.

It is impossible to read the definition of customer as would the Petitioners without doing violence to considerable statutory language. The definition itself refers to "persons *with whom the debtor deals*" (emphasis added) and to persons with "claims" (creditors of the debtor) on account of various specified transactions with the debtor which the Reading Employees never had, and could not have, with respect to the Trust's account. The net equity definition provides for subtraction of "the indebtedness, if any, of the customer to the debtor from the sum which would have been owing by the debtor to the customer". The notion of a conventional customer pervades section

78fff. For example, "customers" are persons to whom the trustee in liquidation is authorized to deliver securities held in their accounts [subd. (c)(2)(B)]; the trustee must give notice of the proceeding to "customers of the debtor as their addresses shall appear from the debtor's books and records" [subd. (e)]; and he must make payments or deliveries of securities directly to the debtor's customers [subd. (g)]. These and other provisions of section 78fff are as obvious as section 60e in their contemplation of the conventional securities customer.

When Congress meant to provide protection based on persons more remote than a debtor's actual customers it did so unequivocally. Thus, although customers who are broker-dealers or banks are denied protection from SIPC's funds, section 78fff(f)(1)(D) specifically authorizes up to $50,000 protection for each of *their* customers on whose behalf they had transactions with the debtor. Each such person is "deemed a separate customer of the debtor". Congress made no similar provision in the case of fiduciary accounts. This was not mere oversight. The 1970 Act recognized that fiduciary accounts are a part of the business of broker-dealers. Thus it provided that a customer who maintains multiple accounts "in separate capacities" shall be deemed a "different customer" in each capacity, and it authorized protection from SIPC's funds up to $50,000 for each capacity.[35] It clearly tied protection to the fiduciary himself, not to the number of his *cestui que trustent*.

The legislative history provides further conclusive evidence of the error of Petitioners' position. Several

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[35] Sections 78fff(c)(2)(A)(iv) and 78fff(f)(1)(B).

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bills preceded the one eventually enacted as the 1970 Act. The four earliest bills were substantially modeled after the FDIA.[36] One of them would have expanded protection beyond $50,000 (up to $250,000) based on "the beneficial interest of five or more natural persons".[37] Two others would have provided $50,000 for each person on whose behalf a customer was "acting as agent".[38] These departures from the concept of limited protection per conventional customer were plainly rejected by subsequent bills[39] and, eventually, the 1970 Act. The legislative history clearly shows that the conventional securities customer was all that anyone had in mind in the class to be protected. During the hearings the terms "customer", "account" and "investor" were used interchangeably by securi-

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[36] S. 2348, and as amended, H.R. 13308, H.R. 17585.

[37] "(5) The term 'insured customer account' means (a) the net amount due any customer from his account maintained with an insured broker or insured dealer, less any part thereof which is in excess of $50,000 or such larger amount as shall be determined by rule or regulation of the Corporation; or (b) the net amount due any institution or entity which represents the beneficial interest of five or more natural persons, less any part thereof which is in excess of $250,000 or such larger amount as shall be determined by rule or regulation of the Corporation". S. 2348, as amended April 9, 1970.

[38] ". . . in the case of a person acting as agent who transacts business for third parties through an account or accounts with a broker, dealer, or member of a national securities exchange, for purposes of the $50,000 limitation, the term customer shall not be limited by the number of such accounts but shall include each such third party insofar as the claims of such third parties are ascertainable from the books and records of either the debtor or the person acting as agent made available to the trustee or are otherwise determined to the satisfaction of the trustee." S. 3988; S. 3989.

[39] H.R. 18458; H.R. 19333; S. 2348 as reported out.

ties industry representatives,[40] members of Congress,[41] the SEC[42] and other representatives of the federal government.[43] The testimony of the then Chairman of the SEC underscores that this legislation was intended to provide $50,000 protection for each securities customer in the ordinary industry sense.[44]

The Petition Before This Court

The Petition is replete with misconceptions of law and unwarranted factual assertions. For example it states (page 13) that Congress gave "little attention" to the definition of customers; states (page 8) that the definition of customer is surrounded by ambiguity; states (page 7) that certain persons associated with the debtor are excluded from the definition of customers;[45]

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[40] Senate Hearings at 11-12, 26-27, 36, 40, 42-45, 178-179, 187, 206, 208-209, 219-220, 225, 227; House Hearings at 166, 306-310, 352-354. A prominent representative of the securities industry referred to risks ". . . run by the investor who may have just walked off Main Street . . . ." Senate Hearings at 42.

[41] Senate Hearings at 142-144, 252-253; House Hearings at 233, 373-374; see also Senate Report at 1-4, 11-14; House Report at 1-4, 8-10. To illustrate, one member of Congress spoke of ". . . the average person picking up the phone, calling his broker . . . ." House Hearings at 233.

[42] Senate Hearings at 8-10, 16, 257; House Hearings at 149-154, 226-228, 230, 328, 333-334, 367-368, 370.

[43] Senate Hearings at 245-246. See also Senate Report at 1-4, 11-14; House Report at 1-4, 8-10; H.R. Rep. No. 91-1788 (Conference Report) 91st Cong., 2d Sess. 1, 24, 26 (1970).

[44] House Hearings at 339-340. See also Senate Hearings at 257; House Hearings at 376, 379-380.

[45] Section 78fff(f)(1)(C) excludes certain associated persons from protection from SIPC's funds, but does not affect the rights of those persons to share in the single and separate fund or the general estate.

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suggests (page 9) that a customer's net equity is not the basis of protection from SIPC's funds; and repeatedly embroiders the facts by referring to the Debtor as the Reading Employees' broker (pages 6, 11), to the Trust account as their account (pages 3, 6), and to their alleged "ownership interest" in the securities or cash in the Trust Account (page 6) which they allegedly had a right to claim (pages 11, 12). Other errors appear,[46] the aggregate of which may have contributed to the Petitioners' ultimate misunderstanding of the term customer as defined in the 1970 Act.

Insofar as the Petitioners contend that each Reading Employee was the separate customer of the

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[46] *First*, the Petition cites (page 8, n. 14) a case as construing the 1970 Act when in fact it construed the definition of customer in section 60e of the Bankruptcy Act. See SEC v. First Securities Co. of Chicago, 507 F.2d 417, 421-22 (7th Cir. 1974). *Second*, it states (page 7) that no case has construed the definition of customer in section 60e when, in fact, the *First Securities* case, *supra*, and others, did. *Supra* n. 21. *Third*, it erroneously suggests that a 1970 Act proceeding is not a true bankruptcy, specifically stating that the debtor's obligations are not dischargeable. The law is otherwise. See section 78fff(e)(1) and discussion at pages 3, n. 4 and 11-13, *supra;* Exchange National Bank of Chicago v. Wyatt, 517 F.2d 453 (2d Cir. 1975); *SEC* v. *Wick*, 360 F. Supp. 312 (N.D. Ill. 1973). *Fourth*, it incorrectly states (pages 8, 14-15) that the issue here is the same as that presented in *In re Weis Securities Inc.* (Claim of McGrath), which involved the interpretation and application of section 78fff(f)(1)(C) which prohibits the use of SIPC's funds, "directly or indirectly", for the benefit of certain persons associated with the debtor. *Fifth*, it erroneously states (page 15) that the 1970 Act is an amendment to the Securities Exchange Act of 1934 ("1934 Act"). Section 78bbb merely makes the provisions of the 1934 Act generally applicable. Compare with section 78ggg(d) which did amend the 1934 Act, and earlier versions of this legislation which would have made the 1970 Act an amendment to the 1934 Act. H.R. 18109, 91st Cong., 2d Sess. §§ 2, 3, 4 (1970); H.R. 18081, 91st Cong., 2d Sess. § 2 (1970); H.R. 18458, 91st Cong., 2d Sess. § 2 (1970).

Debtor, further discussion is unnecessary. The 1970 Act simply was not intended to work a profound metamorphosis whereby these non-customer trust beneficiaries were transmuted into customers of the Debtor.

The Petitioners' alternative position is equally devoid of merit. Although they correctly observe (Petition at 12) that they effected transactions with the Debtor and were the investors or traders, it hardly follows that each was a separate customer of the Debtor within the meaning of the 1970 Act. Only brief discussion is necessary.

By their terms the Plan and the Trust involved here are governed by the laws of Pennsylvania.[47] It is the settled law of Pennsylvania and other jurisdictions that co-trustees constitute but one "collective trustee", that they act in a single joint capacity, and that their powers, interests and authority in the subject matter of the trust are equal and undivided.[48] Plainly the Trustees here maintained a single trust account in a single collective capacity. No one of them had a separate capacity or could be deemed a "separate customer" under section 78fff(c)(2)(A)(iv) or section 78fff(f)(1)(B) of the 1970 Act (discussed *supra* at 13, 15). Together they managed a single trust account which had a single net equity protected to

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[47] Paragraph 12.1 of the Plan provides: "The plan and the trust agreement shall be construed according to the laws of the state of Pennsylvania." Paragraph 8.5 of the Trust agreement similarly provides.

[48] See, *e.g.*, Diviney v. Lynch, 372 Pa. 570 (1953); In re Dorrance's Will, 333 Pa. 162, 166 (1939); Coxe v. Kriebel, 323 Pa. 157, 166-167 (1936); Appeal of Vandever, 8 Watts & S. 405, 405 (Pa. 1845); Hanson v. Birmingham, 92 F.Supp. 33, 42 (N.D. Iowa 1950); Kane v. Lewis, 282 App. Div. 529, 530 (3d Dep't 1953).

$50,000 maximum under section 78fff(f)(1). No amount of legerdemain could support the idea that the amount of protection accorded trust accounts by Congress depends upon such a capricious basis as the number of trustees. The Court of Appeals properly so held.

The Petitioners' pecuniary interest in expanding the definition of customers beyond its terms and intended scope overlooks, among other things, the fact that the 1970 Act was intended only to supply *limited* protection to customers.[49] During the legislative hearings it was recognized that the $50,000 limitation would not fully protect customers with very substantial accounts.[50] The limited protection, in conjunction with other provisions of the 1970 Act, was designed to "restore investor confidence in the capital markets."[51] There was no intention fully to protect against all losses attendant upon the financial collapse of broker-dealers. The decision of the Court of Appeals affords this Trust the full measure of the limited protection intended by Congress. Adoption of either of the Petitioners' contentions by the Court of Appeals would have been judicial legislation tending greatly to enlarge the exposure of SIPC's funds (modest when compared to the FDIC),[52] with potential impact upon

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[49] See, *e.g.* SEC v. Packer, Wilbur & Co., Inc., 498 F.2d 978, 983 (2d Cir. 1974).

[50] See, *e.g.*, House Hearings at 339-340.

[51] SIPC v. Barbour, 421 U.S. 412, 415 (1975).

[52] At December 31, 1975 the SIPC Fund [as defined in section 78ddd(a) *et seq.*] totalled $87,562,946. 5 SIPC Ann. Rep. 19 (1975). The minimum congressional objective was to build the Fund to 150 million dollars, after which assessments on SIPC's broker-dealer members may be reduced. See section 78ddd(d)(1). It was thought that objective would be achieved in five years. Senate Hearings at 243; House Hearings at 346. It has not.

funds of the United States and a resulting increased burden on the securities industry as well as investors in equity securities.[53]

CONCLUSION

Respondent Securities Investor Protection Corporation respectfully submits that the petition for a writ of certiorari should be denied.

Respectfully submitted,

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[53] If SIPC's funds should become insufficient to meet the purposes of the 1970 Act, up to 1 billion dollars may be borrowed by SIPC from the United States Treasury. Section 78ddd(g)-(h). These funds must be repaid. *Ibid*; see also section 78ddd(f). Such repayment may involve both an increase in the assessments on SIPC's broker-dealer members [section 78ddd(d)(1), (f) and (g)], and the imposition of a transaction fee upon certain purchasers of equity securities. Section 78ddd(g). During the congressional hearings, the then Under Secretary for Monetary Affairs expressed concern regarding a possible drain on funds of the United States. See Senate Hearings at 242-244; House Hearings at 344-347. It was hoped that the SIPC Fund derived from assessments on broker-dealers would be sufficient and "self-sustaining" to carry out the purposes of The 1970 Act. *Ibid.* The Secretary of the Treasury and the Federal Reserve Board are both represented on SIPC's Board of Directors. Section 78ccc(c)(2)(A) & (B).